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Capital Is the Landlord

*Class-Monopoly Rent and New Geographies
of Subprime and Predatory Mortgage Lending*

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Capital is the Landlord: Class-Monopoly Rent and New Geographies of Subprime and Predatory Mortgage Lending

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Abstract: The debate over “subprime” and “predatory” home mortgage lending has become a central theme in urban research, housing policy, and community activism. Most contributions to this debate have followed the disciplinary traditions of applied economics and housing policy analysis, however, and have therefore obscured geographical dimensions of the process while privileging demand-side questions (such as the financial circumstances or utility-maximizing choices that lead consumers to agree to abusive loan terms). In this paper we place the focus on the supply side, with an analysis of the institutions responsible for the flow of subprime and predatory mortgage capital into America’s working-class and minority neighborhoods. Our analysis relies on some of the conventional methods of contemporary housing research, but draws theoretical force from a stream of urban theory that has been neglected in recent years. In the 1970s and 1980s, vibrant interdisciplinary debates surrounded David Harvey’s theoretical and empirical work in Baltimore, where he portrayed a network of hierarchically-structured financial institutions and government policies creating a local framework for the realization of class-monopoly rent in segmented housing submarkets. In the last two decades, however, class-monopoly rent has been reconfigured by policy, activism, and structural changes in American housing finance. We analyze how the simultaneous growth of securitization and subprime and predatory lending is replacing familiar landlord-tenant relations with new class-monopoly relations between homeowners and the institutions and individuals working in increasingly sophisticated capital markets. Our empirical analysis is based on evidence from the Baltimore-Washington metropolitan region between 1998 and 2002. Quantitative analysis of mortgage lending records is used to describe the changing institutional face of subprime mortgage capital, its racial-geographic biases, and its integration into secondary-market investment networks. Qualitative case studies of prospectus materials shown to investors who buy subprime mortgage-backed securities allow us to trace the connections between capital markets and localized patterns of subprime market segmentation. Our evidence suggests that class-monopoly rent has been geographically reconstructed: the use value of the home remains necessarily localized, but the flows of money required to finance have created a complex web of payments to various individuals and institutions operating at various scales. The exposure of localized class-monopoly rents to national and transnational capital markets presents new challenges for regulation and the community reinvestment movement.

Introduction

“Securitization has let us bring in vast amounts of capital from the national and global markets.”

Steve Nadon, Chairman of the Coalition for Fair and Affordable Lending, and Chief Operating Officer of Option One Mortgage (Nadon, 2003, p. 3).

“This truly amazing mortgage structure, based on an international secondary market, has given the American population the best, cheapest, and most efficient mortgage capital delivery system in the world. This highly functional secondary mortgage market is, however, greatly dependent on legal certainty and predictability. In short, secondary market investors must have the security of being able to purchase and trade mortgage-backed assets without undue complications and without excessive legal risk.”

Robert Couch, Chairman of the Mortgage Bankers Association (Couch, 2003, p. 6).

“All of these institutions ... operate together to relate national policies to local and individual decisions, and in the process create localized structures within which class-monopoly rents can be realized.”

David Harvey (1974, p. 259).

“These are the knuckle-breakers of the business.”

A Moody's bond-rating analyst, describing a specialized subprime loan servicing company (quoted in Cohen, 2000).

Predatory home mortgage lending ~ the use of deceptive tactics to pressure borrowers into exploitative, high-cost credit ~ has exploded in the last decade, and has become a central theme in academic research, public policy, and community advocacy. Enormous debate has centered on distinguishing predatory practices from legitimate activities in the subprime or “B-and-C” market, a sector that involves higher-cost loans made to people with blemished credit histories or other risk factors. This debate has clear relevance for advocacy and policy, illustrated most starkly by Phil Gramm’s reasoning that legislation is unnecessary because “As the regulators themselves admit, there is no definition of predatory lending. I don’t know how we can hope to address the problem before we have decided what it is.”¹ (quoted in Heller and Garver, 2000, p. 1). Yet Gramm, who holds a doctorate in economics, clearly understood the fundamental theoretical implications: the torrential flow of evidence of widespread predatory practices strikes at the heart of contemporary neoclassical theories of housing and credit markets. How can any rational, utility-maximizing consumer accept loans on the kinds of terms that have been documented in thousands of news stories and court cases? Why would a rational, profit-maximizing lender advance a loan that is almost certain to lapse into delinquency, default, and foreclosure? These questions are the focus of a growing body of research at the nexus of economics, law, and housing policy, which has shown how the economic incentives of mortgage lending have been altered by changes in the financial services market interacting with the historical legacy of credit rationing and discrimination. Even the most rational consumer can be tricked into an abusive loan, and now even quite risky loans can be made profitable for lenders, brokers, contractors, secondary-market investors ~ everyone, that is, except for the borrower (Apgar et al., 2004; Eggert, 2003; Engel and McCoy, 2002; HUD-Treasury Joint Task Force, 2000; Squires, 2003).

Unfortunately, geographical processes have been obscured or overlooked in much of this debate. It is well understood that subprime and predatory lending are concentrated in minority and working-class neighborhoods.

¹ Engel and McCoy (2002) provide the most rigorous and systematic definition of predatory lending as a syndrome involving one or more of the following: loans structured to result in seriously disproportionate net harm to borrowers; harmful rent-seeking; fraud or deceptive practices; other forms of lack of transparency that are not legally actionable as fraud; and loans that require borrowers to give up meaningful legal redress.

Yet the prevailing interpretation of these patterns is fundamentally economic and demand-side: subprime segmentation is seen as nothing more than an industry response to the spatial distribution of borrowers with credit histories or other characteristics that make them prime candidates for higher-cost loans. In this paper, we seek to place the focus on the supply side, with an analysis of the kinds of institutions involved in subprime and predatory segments of the home mortgage market. Although we rely on some of the standard econometric methods of the mainstream housing policy literature, the theoretical foundations of our work come from David Harvey's (1974) framework connecting local housing submarket inequalities to the dynamics of national capital accumulation. Our analysis documents how a convergence of forces in capital investment, public policy, and community activism have restructured the relations between national and transnational capital markets and neighborhood class relations in housing markets. Class-monopoly rent, a central feature of the racialized inner-city tensions of the late 1960s and early 1970s, has been reconfigured in ways that create troubling new inequalities while putting a new institutional face on old ones.

The paper is structured as follows. In the next two sections, we outline Harvey's theory of class-monopoly rent and its relevance for understanding the geographical dynamics of today's wave of subprime and predatory mortgage lending. We then sketch a descriptive portrait of the changing institutional face of mortgage lending and its geography. The next section develops a multivariate model of market segmentation, an essential step in the effort to distinguish demand-side factors from supply-side strategies of institutional structure and target marketing. Model results indicate that demand-side characteristics offer a poor explanation of market segmentation, which is more closely tied to the expansion of large, specialized organizations targeting minority borrowers while accessing the expanded capital sources of the secondary market. We then provide alternative views of the spatial disparities of subprime mortgage capital as a whole, and of several case study lenders working the connections between transnational capital markets and local neighborhood processes of subprime and predatory lending in Baltimore (the site of Harvey's empirical work in the early 1970s). We conclude with a consideration of the implications for recent trends in urban theory, public policy, and community organizing.

Harvey's Contribution

In the early 1970s, the publication of several theoretical and empirical pieces by David Harvey launched a broad, interdisciplinary debate on the relationship between urban social problems and the dynamics of the circulation of capital. This research agenda continued well into the 1980s, as Harvey elaborated comprehensive theories of the geography of capital accumulation (Harvey, 1982, 1985). For our purposes, however, the definitive source for understanding the historical roots of today's dilemmas of predatory lending is an article that grew out of one of Harvey's earliest projects in Baltimore (Harvey, 1974). Inspired by Henri Lefebvre's (2003 [1970]) theorization of a fundamental urban revolution in the development of capitalism,² Harvey (1974) was encouraged to reconsider conventional theories of land rent as a way of gaining insight into contemporary urban problems. In classical economics, rent is simply a transfer payment that helps to allocate a scarce natural resource (land) among competing uses in order to promote efficient production. But rent is inherently social, because "actual payments are made to real live people and not to pieces of land. Tenants are not easily convinced that the rent collector

² Harvey's (1974) article offered the first sustained evaluation of Lefebvre's provocative argument that the "urban revolution" of the twentieth century had transformed struggles over economic growth and industrialization into fundamentally urban questions ~ the "urban problematic" (Lefebvre, 2003 [1970]). Industrial capital in the nineteenth century was able to "conquer the city, penetrate it, break it apart, and in so doing extend it immeasurably, bringing about the urbanization of society..." (p. 13). "The urban problematic becomes a global phenomenon.... Urban reality modifies the relations of production without being sufficient to transform them. It becomes a productive force..." (p. 15). Lefebvre had also proposed that "the proportion of global surplus value formed and realized in industry declines" while the share formed "in speculation, construction, and real estate development grows." (cited in Harvey, 1974, p. 250). Harvey was intrigued by this notion, offered almost in passing, of separate but interrelated primary and secondary "circuits of capital," and in later works he developed full-fledged theoretical frameworks to explain the dynamics of circuit-switching (Harvey, 1982, 1985; see also Beauregard, 1994).

merely represents a scarce factor of production” (p. 251). Moreover, rent can only be realized through exclusive control of land, protected by the institution of private property, and the scarcity that confers value to land is itself created by urbanization ~ making it “difficult to distinguish between rent and profit.” (p. 252). Gaining access to the economic benefits of urban land, then, requires some degree of monopoly control backed up by class position and the force of law. “Class-monopoly rents arise because there exists a class of owners of ‘resource units’ ~ the land and the relatively permanent improvements incorporated in it ~ who are willing to release the units under their command only if they receive a positive return above some level.” (p. 253). This kind of class analysis is a hallmark of historical studies of nineteenth-century industrialization and conflicts between landowners and an emergent capitalist class, but Harvey’s concern in the late 1960s and early 1970s involved tensions between a) landlords and low-income tenants in the inner city, and b) speculator-developers and middle- and upper-income households in the expanding suburbs. The outcome of these tensions depends, in large part, on the mechanisms available to different groups “for expressing their collective class interests,” (p. 256) ranging from zoning, planning, and housing regulations, to the strength of political organization or patronage networks. But one of the crucial mechanisms shaping these local conflicts is a national institutional framework for the allocation of capital and credit: Harvey postulated “an hierarchical structure of some sort through which class-monopoly rents percolate upwards but not downwards. At the top of this hierarchy sit the financial institutions.” (p. 257).

This hierarchy implicates national and global capital flows, then, in a variety of local urban processes ~ such as the relations between tenants and landlords, middle-class residents and developers, debt-encumbered homeowners and the banks holding their mortgages:

“...in the United States, the main mechanism for coordinating national and local, individual and societal activities lies in the hierarchical structure of financial institutions operating under governmental regulation. This structure is exceedingly complex, and I shall not attempt to detail it here. It is important to note one feature of it, however. Certain kinds of institution ~ the state and federally chartered savings and loan institutions ~ operate solely in the housing sectors. They were initially designed to ‘promote the thrift of people locally to finance their own homes and the homes of their neighbors.’³ Some of these institutions operate on a non-profit basis. They are, of course, affected by money market conditions and governmental regulation. These institutions contrast with the mortgage banks, savings banks, and commercial banks which are oriented to profits or to the expansion of their business. All of these institutions, however, operate together to relate national policies to local and individual decisions, and in the process create localized structures within which class-monopoly rents can be realized.” (Harvey, 1974, p. 259).

We contend that this hierarchical structure has been reconfigured, pulling class-monopoly rent out of its localized context and weaving it into networks of lending industry subsidiary structure and secondary-market purchasing networks. Class-monopoly rent has been partially torn from its local roots, reproducing race- and class-stratified housing submarkets through new and sophisticated institutional arrangements. The rise of a fully-articulated secondary mortgage market has replaced Harvey’s (1974) inner city landlord-tenant relation with a web of (partially) despatialized relations between investors and an expanded class of debt-encumbered homeowners saddled with high-cost loans. Capital has become the landlord.

Subprime and Predatory Lending and the Transformation of Class-Monopoly Rent

For anyone familiar with recent discussions of subprime and predatory lending, Harvey’s (1974) account of the housing finance system appears in an almost nostalgic light, viewed across a rough and complex terrain of

³ Harvey at this point includes a reference to a companion paper (Harvey and Chatterjee, 1974), which includes a discussion of the divergent regulatory structure and missions of State and Federally chartered savings and loan institutions.

legislation, industry restructuring, and community activism over the last thirty years. There is an enormous literature that maps out this landscape of changes, and we make no attempt to provide a comprehensive review here (see Apgar et al., 2004; Dymski, 1999; Engel and McCoy, 2002; HUD-Treasury Joint Task Force, 2000; Retsinas and Belsky, 2002; Ross and Yinger, 2002; Squires, 1992, 2003). But there are several landmarks on this terrain that are critical for any understanding of today's geography of high-cost, high-risk credit markets. In this section we outline the institutional transformation of American housing finance over the last generation, and then we examine how this shift has altered localized relations of class-monopoly rent.

Through the 1960s, home mortgage lending in the United States was dominated by banks and locally-oriented thrift institutions operating under tight regulations on the spatial extent, range of products, and costs of funds available to lend. This regime, established during the 1930s with periodic adjustments, is often portrayed as something of a "golden age" in which borrowers, savers, and bankers all knew each other and lived in the same neighborhood. But the system was premised on, and in turn reproduced, severe forms of racial and class segregation. The system was also vulnerable to information asymmetries that led lenders to ration the volume of credit rather than its price, thereby denying loans even to many qualified borrowers (Stiglitz and Weiss, 1981). The late 1960s and early 1970s began a period of dramatic change in this regime (see Dymski, 1999; Engel and McCoy, 2002). Fair housing legislation in the 1960s sought to address the entrenched legacy of racial discrimination against African Americans and other minorities, and legislative amendments in 1968 redirected the once-discriminatory programs of the Federal Housing Administration (FHA) to serve lower-income, first-time homebuyers (Wachter, 1980). A few years later anti-redlining activists succeeded in mandating public disclosure of certain lending data (the Home Mortgage Disclosure Act of 1975) and in requiring lenders to provide credit equally to all areas from which they accepted deposits (the Community Reinvestment Act of 1977). Severe inflation and imbalances in short- and long-term interest rates led to Congressional action relaxing some of the old restrictions on home mortgage lenders, thereby encouraging a proliferation of many new types of loan products.⁴ Regional bottlenecks in interest rates and other signs of capital shortages in the housing sector prompted the creation of a national secondary market, led by the large Government Sponsored Enterprises (Fannie Mae and Freddie Mac); by the late 1980s, most home loans were sold on the secondary market shortly after origination, providing lenders with a steady stream of new capital to lend. Securitization eroded one of the binding constraints of credit rationing, allowed new types of thinly-capitalized 'non-bank' lenders to expand their market share, reduced the cost of funds, and led to a flood of capital into the home mortgage business (Apgar et al., 2004; Engel and McCoy, 2002; Squires, 2003). Simultaneous advances in the sophistication of loan modeling, credit scoring, and borrower behavioral modeling solved some of the information asymmetries facing lenders. Further market information was provided by the loan performance histories of subsidized FHA programs, with some of the most risky programs providing the most valuable market intelligence. In the wake of major legislation in the wake of the savings and loan crisis of the 1980s (amendments to HMDA and CRA in 1989, regulatory changes affecting the GSEs in 1992), the first year of the Clinton Administration brought a major push to enforce fair housing legislation and expand homeownership to racial and ethnic minorities, low- and moderate-income (LMI) households, and inner-city neighborhoods. The combined effects of community activism, regulatory response, and the lure of profit had eroded an old system of exclusionary redlining; in its place has come a more complex, stratified system of credit market segmentation:

The changes in home-mortgage markets have made it possible for borrowers of all risk levels to work with an array of different loan originators and select from a menu of loan products offered

⁴ Engel and McCoy (2002, p. 1275) describe how the Depository Institutions Deregulation and Monetary Control Act (DIDMCA) of 1980 preempted state usury limits on interest, discount points, and other charges on loans backed by first-mortgages homes, such that "lenders who wanted to charge higher rates had new incentives to refinance first mortgages," rather than state-regulated subordinate liens; and how the Alternative Mortgage Transactions Parity Act (AMTPA) of 1982 "preempted old restrictions that limited lenders to making fixed-rate, amortizing mortgages. As a result, lenders received the green light to make adjustable-rate mortgages, mortgages with balloon payments, and non-amortizing mortgages where borrowers pay off the interest but not the principal."

by both prime and subprime lenders. An irony of these market changes is that they have contributed to the emergence and success of predatory lenders. Conceivably, predatory lenders now can originate predatory loans in LMI neighborhoods and sell them to private secondary participants and, conceivably, the GSEs.... Likewise, they can find potential loan purchasers among banks that seek to fulfill their CRA obligations by purchasing loans made to LMI borrowers. Similarly, predatory lenders can make predatory, FHA-insured loans and insulate themselves somewhat from the cost of defaults. Lastly...AMTPA has enabled predatory lenders to peddle complex and predatory-loan products that are difficult for inexperienced and unsophisticated borrowers to understand. (Engel and McCoy, 2002, pp. 1277-1278).

All of these changes have reconfigured the spatial, institutional, and individual facets of class-monopoly rent. Direct monopoly ownership control of the scarce resource of urban land and improvements, as exemplified in the inner-city landlord-tenant relation, has been overshadowed by struggles for access to credit on favorable terms, which is based on class divisions in intergenerational wealth transfers, investments in education, and discrimination in housing and labor markets. Differential access to credit then helps to determine who gains access to capitalized assets (homes) with good prospects for appreciation and further wealth accumulation. After a generation of policy, activism, and market shifts that have increased homeownership in working-class and racially marginalized neighborhoods, the old landlord-tenant relations are giving way to contemporary versions of “housing classes” (Rex and Moore, 1967) shaped by the intricate rules of mortgage debt.

The landlord’s extraction of surplus value from renters is replaced by a multifaceted web of interactions where actors in the capital markets make claims on debt-encumbered homeowners. Anyone who borrows money to buy a house, or who taps accumulated home equity to pay off other debts, is essentially renting capital from the mortgage-finance system, while putting at risk their property rights over a home. For those with access to the increasingly competitive prime mortgage market, the rent payment to borrowed capital is quite reasonable (particularly in these times of low interest rates), apparently undermining the relevance of any ideas of class-monopoly rent.⁵ But for those who are shut out of the prime market, the payment can be quite substantial, and thus a critical line of debate in the literature involves the question of whether borrowers freely choose predatory loans or are forced into them by aggressive marketing and sales tactics.⁶ The class-monopoly aspects of this rent payment, however, are obscured for two key reasons. First, even the most heavily indebted borrowers are still considered homeowners, and we must not disrespect the desperate struggles of many predatory lending victims who work to meet oppressive payments month after month in the hopes of keeping their homes. Second, the rent payment has been fragmented and partitioned, a reflection of the complex fragmentation of the mortgage instrument itself. At the local scale, parts of the landlord-tenant rent payment are now claimed by fraudulent home repair contractors, mortgage brokers, realtors, and appraisers who work together to peddle complex predatory loan schemes. Another share is claimed by lenders ~ either small local mortgage companies, or local branches of large national firms created by the merger wave of recent years ~ who earn substantial revenues from high interest rates as well as discount points, hidden charges, and the “packing” of extras such as single-premium credit life insurance. When the lender sells the loan on the secondary market to get a fresh infusion of capital to lend, the borrower’s rent payments are suddenly redirected to a new note-holder, who is likely to represent a pool of mortgage-backed securities offered on one of the national exchanges. If the servicing rights are sold to a

⁵ The intense competition of prime lenders in high-income submarkets, even in the absence of large monopoly rents from individual borrowers, generates respectable fee income while (in times of falling interest rates) cannibalizing the returns of other investors (who hold the original loans being refinanced). Moreover, lenders compete in these markets to provide a broad range of insurance, borrowing, and investment services to their preferred customers. The image of a “one-stop shopping” option for financial services was a key argument in the industry push to repeal Depression-era banking and securities firewalls in the Gramm-Leach-Bliley Financial Services Modernization Act of 1999.

⁶ In a widely-publicized study that attracted predictable industry criticism, the Coalition for Responsible Lending (Stein et al., 2001) estimated that predatory practices cost borrowers more than \$9 billion annually.

separate entity, then this company will claim another share of the borrower's rent payments to capital.⁷ Securitization tears parts of the class-monopoly rent relation out of its local context, to be sure, but it also severs the *individual* ties of the payments made for the privilege of renting capital: in the secondary market, we can no longer identify the individual who extracts surplus value from a homeowner who is renting capital on subprime or predatory terms. Beneficiaries include investment bankers, loan servicers, and thousands of investors who buy shares of mortgage-backed securities. It is important to understand the motivations and conflicts among all of these agents, to be sure. They do not constitute a faceless, anonymous entity. And yet their actions are inextricable from the incentives of capital accumulation.

We suggest that homeowners in subprime or predatory lending relationships exemplify the transformation of class-monopoly rent, as local housing market tensions are woven much more closely into capital-market flows at the national and transnational scale. The resulting framework is not a tidy, hierarchical system, and there are many examples of important transnational webs that cut across the more easily-recognized path from Main Street to Wall Street.⁸ But the implications of class-monopoly rent are considerable, in light of the enormous flows involved. The total number of subprime home loans exploded from 104,000 in 1993 to nearly a million five years later (HUD-Treasury Joint Task Force, 2000). The volume of all mortgage-backed securities issued in 2002 approached three-quarters of the total mortgages originated that year, with total outstanding MBS of some \$3.8 trillion. Indeed, the securitization of home loans has moved to center stage in national and transnational debt markets, as the securities issued by Fannie and Freddie have come to replace the Treasury's old 30-year "long bond" after its retirement in late 2001.⁹

The Culture of Mortgage Capital

Class-monopoly rent should not be mistaken for an economic determinism that portrays all of these processes as inevitable, unitary, and coordinated. Harvey's reading of capital in the built environment was widely regarded as a functionalist, economic, and deterministic account devoid of cultural depth or human agency. Many of Harvey's contemporary critics, to be sure, were responding to simplified caricatures or decontextualized versions of circuits, switches, and crises.¹⁰ Yet in a familiar if troubling historical paradox, policy and practice trumped theoretical debate: many urban theorists turned away from political economy to cultural analysis in the years when policy was recast in terms of economic entrepreneurialism, privatization, and the aggressive use of market forces in nearly all domains of social and economic policy (Lake, 2002; Osborne and Gaebler, 1993; Peck and Tickell, 2000; Wacquant, 1999). Nevertheless, the triumph of market forces was by no means divorced from changes in cultural practices in the 1990s. As culture was further commodified, capital itself seemed to acquire culture, taste, and sophistication. Capital became a legitimate theme in all sorts of conversations. Capital became

⁷ Loan servicers make most of their profits from late charges and other fees, creating incentives for these companies to delay posting payments or use other tactics to trigger penalties (Eggert, 2003, 2004).

⁸ The clearest illustrations of transnational connections involve bank competition to gain a share of the money-transfer fees associated with the \$13 billion in annual remittances sent home by Mexicans working in the U.S. Two companies have begun programs to allow Mexican workers in the U.S. to apply for a loan to buy a home in Mexico while making payments in U.S. dollars through an American bank (Malkin, 2004).

⁹ The increasing popularity of the GSE securities has become a subject of heated debate in Washington, since investor sentiment is based on an implicit assumption that the federal government would not allow the failure of trillion-dollar enterprises. Among the many critics is Alan Greenspan, whose latest warnings about this "implied subsidy" came in a February 2004 appearance before the Senate Banking Committee, where he noted that "There is a general belief in the marketplace that these securities are backed by the full faith and credit of the United States government," (quoted in Andrews, 2004) which was of course the traditional function of the long-bond before its demise after a few years of budget surpluses prompted concerns of a shortage of Treasury-backed debt instruments that would serve as a benchmark for other types of debt. Greenspan has been concerned about the rapid growth of the GSEs and vulnerabilities in their ability to hedge interest rate risk.

¹⁰ In this sense we concur with Beauregard's (1994, p. 729) assessment: "...Harvey cannot be typecast as an economic determinist. Even in his earliest writings on capital switching he was aware of the role of financial intermediaries and, in later works, has also been sensitive to social, political, and cultural forces...."

cool. Bar-rooms re-tuned their televisions from ESPN to CNN or MSNBC. The morning check of the stock portfolio and the 401k became an upper-middle class obsession, and the pastime began to work its way down the class ladder. Henry Blodget, Mary Meeker, Jack Grubman, and dozens of other stock analysts emerged from obscure securities industry occupations to become familiar media celebrities, and even the staid figure of Alan Greenspan gained a cult of followers who parsed every policy statement and turn of phrase (from “irrational exuberance” in 1996 to “infectious greed” amid the corporate scandals of 2001-2002).¹¹

These trends have direct relevance for homeownership and mortgage markets. On the one hand, it is impossible to ignore the pure, brutal portfolio logic of capital flooding into housing finance and mortgage-backed securities over the last two decades, given the powerful role of these instruments as portfolio hedges (Caplin et al., 1997). For years, economists have expressed deep reservations over the many ways that tax policies and other implied subsidies lead to systematic overinvestment in real estate, thereby distorting the optimal, efficient allocation of capital among alternative investments (Aron, 1972; Hendershott and Hu, 1980; Green and Reschovsky, 2001). Although the histories of subsidies for housing construction and commercial/industrial real estate are uneven and complex, the tax incentives for homeownership have been durable and generous, exceeding by some estimates \$100 billion annually by the end of the 1990s (Dreier, 2001, p. 71). The increasing sophistication of secondary mortgage markets simply expanded the opportunities for investors to tap into different components of homeowner subsidies.

Yet these brutally economic incentives for investors are at once social and cultural: tax concessions to homeownership have only the weakest economic rationale, and instead draw legitimacy from a powerful incarnation of cultural policy that emerged in the mid-twentieth century American political economy (Hayden, 1984; Wright, 1981). In the popular and political imagination, subsidies to homeownership are never defined that way: imputed rent and tax deductions are seen as entitlements, as nothing more than a recognition of the American exceptionalist traditions of individualism, self-reliance, private property, and home. This nearly universal interpretation can be traced back to the late 1940s, but its resonance and contextual significance have changed with each generation. The distinction of the 1990s was the broad consensus achieved on the virtues of capital and markets in attempts to solve various kinds of social problems. Homeownership became a central avenue of consensus among Democratic and Republican legislators, inside-the-Beltway politicians and devolutionary states’-rights advocates, Brooks-Brothers bankers and on-the-streets community organizers. Mortgage policy became an ever more important means of intervening in housing markets: even the most abstract economic theories or the most obscure regulatory provisions could (if the need arose) be justified on the basis of the unassailable invented traditions of American homeownership.

¹¹ Even in the terrorized recessionary years of 2002 and 2003, the financial pages continue to generate a steady stream of images of bizarre ironies of the culture of capital. Two recent examples make the point. In 2002, Henry Blodget (former star stock analyst at Merrill Lynch) paid \$4 million in fines and was banned from working in the securities industry; a year later, he was hired by the online magazine *Slate* to cover the insider trading trial of Martha Stewart. His first article submission came with a disclosure statement that one reporter dubbed “a classic of the genre.” “Like Martha,” Blodget wrote, “I have had the bizarre experience of watching legions of people I have never met come to trust me, look to me for guidance, regard me as a ‘guru,’ and then decide that I am, in fact,” a scoundrel (Carr, 2003, p. C8). And of course the cultural significance of corporate reputations now routinely extends into the realm of sexuality and pornography. *Playboy* has run features of the ‘Women of Enron,’ as well as the ‘Women of Wal-Mart’ (Bhatnagar, 2003). *New York Times* columnist Frank Rich (2003) makes the link explicit, arguing that media attention to the CEO scandals of recent years is nothing short of pornographic: some of the raunchiest scenes appear in the video of an extravagant \$2 million birthday party that L. Dennis Kozlowski arranged for his wife on Sardinia. Kozlowski stands accused of looting hundreds of millions of dollars from Tyco International, and portions of the Sardinia video were shown to jurors at his fraud trial. It’s tasteless, but Rich suggests that “we want to see these videos anyway. Their pull has to do with capital, not carnality. Money remains the last guilty pleasure in America. The obscenely rich engaging in conspicuous consumption or conspicuously idiotic behavior is the only excess that hasn’t lost its power to amuse, titillate and shock.” (Rich, 2003, p. 1).

The Clinton Administration's fair lending initiative, launched in 1993, was shaped by these political and cultural circumstances (see Squires, 1992, 2003; Vartanian et al., 1995). Conceived as a delayed enforcement of civil-rights legislation that had languished on the books since the 1960s, the initiative was also designed to increase credit and homeownership among inner-city residents, racial and ethnic minorities, and other "underserved markets." For several years, the effort incited hostile debate among economists, regulators, community activists, and banking industry analysts: the entire policy was premised on the idea that markets could be imperfect and in need of substantial intervention, and on the fact that bigotry and discrimination persisted in many parts of the industry. But even the most aggressive and well-funded efforts to defend the status quo were forced into a defensive posture, wielding an abstract economic argument: discrimination is an economically irrational forfeiture of profits, and therefore competitive markets will destroy any firms that engage in these suboptimal practices. Advocates of regulation and enforcement could appeal to the American Dream.

The Washington-Baltimore Region

To evaluate our arguments on the changing spatial and institutional character of class-monopoly rent, we conducted an empirical study of mortgage lending patterns in the Washington and Baltimore metropolitan areas (Figure 1). Our empirical analysis is designed to test three hypotheses. First, we propose that subprime and predatory lending, fueled by changes in the institutional structure of housing finance and the expansion of the secondary market, has been targeted at those working-class and minority neighborhoods that have traditionally suffered from discrimination, redlining, and disinvestment. Second, we hypothesize that "choice," at least as measured in terms of demand-side characteristics of borrowers, is an inadequate, limited way of understanding the rise of subprime and predatory lending; instead, we propose that the new geography of class-monopoly rent is best understood in terms of the strategies and characteristics of lenders. New types of lenders, and new subsidiaries of established lenders, are actively targeting particular groups of homeowners and homebuyers. Third, we hypothesize that subprime and predatory capital has a clear spatiality that cannot be understood solely in terms of the economic dimensions of supply and demand. Housing and credit market segmentation help to sustain localized frameworks conducive for accumulation. We suggest that the institutional transformation of the last thirty years has not entirely erased the patterns of segmentation documented by Harvey's work in the early 1970s; but we also contend that it is possible to trace some of the new connections between local predatory practices and national and transnational capital markets.

Our evidence is drawn from the annual releases of loan records and lender characteristics from the Home Mortgage Disclosure Act (FFIEC, annual), a classification of subprime lending institutions developed by researchers at the U.S. Department of Housing and Urban Development (Scheessele, 2003), and from investor prospectus materials disclosed as part of Mortgage-Backed Securities deals. We chose the Baltimore-Washington study area to permit a comparison of Harvey's extensive Baltimore work with present-day conditions ~ in the context of an exceedingly rich tapestry of broader regional patterns. Housing quality submarkets run across an impressive spectrum, from multi-million dollar suburban mansions (especially in Maryland's exclusive Potomac and Virginia's Maclean) to aging mid-twentieth century inner-ring suburbs of mid-tier and now middle-aged housing stock, to modest outlying rural districts woven into the metropolitan economy by middle-income commuters in search of affordable new single-family homes (especially Frederick and the "panhandle" counties of eastern West Virginia), to clusters of vacancy chains and demolitions in Northeast Washington, Anacostia, and West Baltimore. And the region is also shaped by intricate patterns and processes of choice and constraint in terms of class, racial-ethnic, and immigrant diversity. Historic divisions between Washington's (white, wealthy) west and (black, poor) east, and between Baltimore's elite northern wedge and its other residential districts, have pushed ever farther outward in sectors of intraurban migration and investment through successive waves of uneven suburban development.

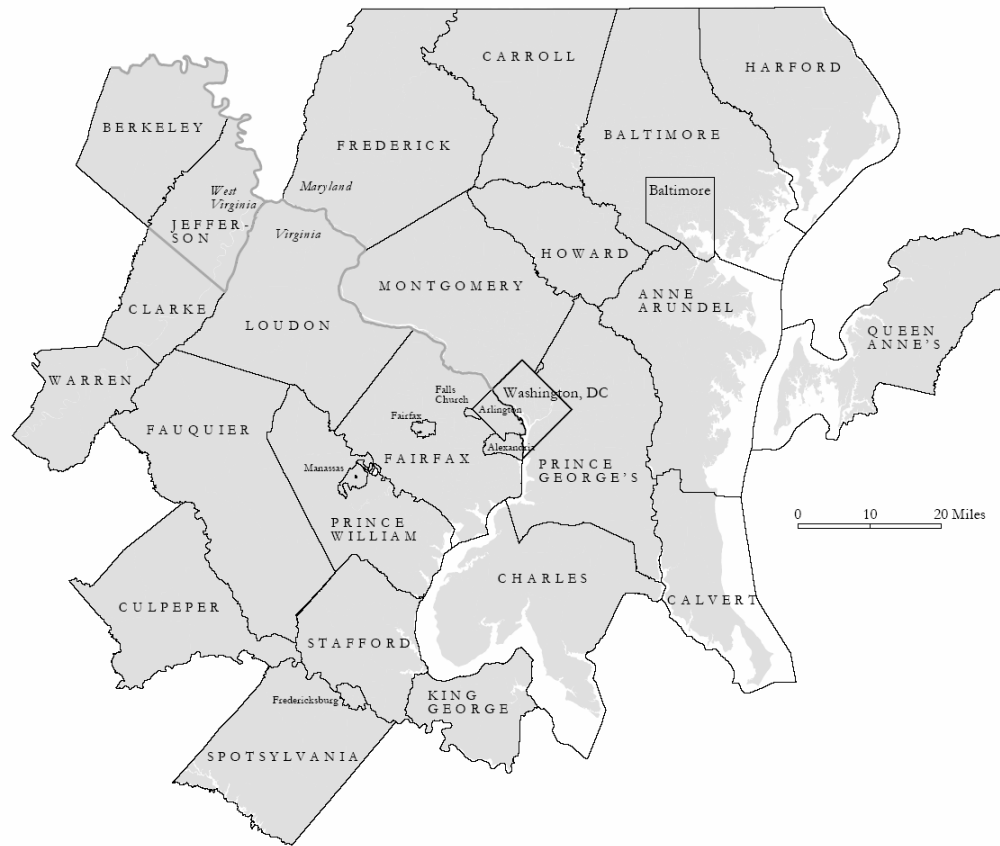


Figure 1. Washington-Baltimore Study Area.

A First Glance at Institutional Change

We begin our empirical analysis with a descriptive portrait of the types of institutions responsible for the subprime boom, and a series of maps updating Harvey’s (1974) maps of the segmented Baltimore housing market. Our analysis documents a turbulent period (see Tables 1, 2, and 3). Between 1998 and 2002, conventional purchase requests increased by 60 percent, while renovation activity declined slightly after a peak in 2000; refinance activity fell by half from 1998 to 2000, before quadrupling to 578 thousand requests in 2002. The composition of these market flows highlight several trends. First, consistent with scores of previous studies, subprime business is more common in the home improvement and refinance markets. Among home purchase requests, subprime market share increased from 7.9 percent in 1998 to 10.6 percent in 2000, before sliding back to the 8 percent range (Table 1). In the refinance market, subprime share steadily increased (from 16 percent to 31 percent) (Table 2). In refinance these trends are complicated by rapid jumps in prime demand whenever interest rates fall; subprime refinance share reached its peak (44 percent) in 2000, even as absolute volume was falling amid mounting credit risks and a variety of other industry problems (Table 3). The spatial imprint of subprime penetration in the refinance market (Figure 2) highlights the combined effects of racial and class divisions, with the highest rates in the city of Baltimore, the eastern half of the District, and Prince George’s County. The lowest subprime shares trace out the wealthiest suburbs directly north of Baltimore, the exclusive Maryland suburbs northwest of Washington, and most of Virginia’s Fairfax and Loudon Counties.

Second, the industry remains broadly partitioned between depository lenders ~ those for whom mortgage lending is often only one of many lines of business ~ and companies that exist solely to make home loans. Prime activity is spread across a variety of competitors, and there is a strong representation of lenders with some connection to depository functions and the associated community ties and federal regulations. A smaller range of lender types

compete in the subprime market; in the lucrative refinance market, independent mortgage companies remain dominant.

Table 1. Industrial Segmentation, Conventional Home Purchase Market.

	(a) Subprime institutions.				
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	0.0	1.0	1.9	1.7	4.8
Bank (FRB)	2.1	1.5	0.0	0.1	0.2
Bank (OCC)	0.8	2.5	25.4	26.1	13.5
Thrift	11.1	10.9	5.5	3.2	1.2
Credit union	0.0	0.0	0.0	0.0	0.0
<i>Mortgage companies</i>					
Independent	77.8	57.4	31.6	38.6	56.7
Owned by bank	2.0	20.3	25.7	22.9	18.8
Owned by holding company	6.1	5.7	9.5	7.0	3.9
Owned by thrift or credit union	0.2	0.7	0.3	0.4	0.9
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
 (b) All others, excluding manufactured home lenders.					
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	3.8	3.7	4.5	3.7	4.4
Bank (FRB)	1.8	2.3	1.8	2.1	2.6
Bank (OCC)	6.8	12.2	16.1	14.6	11.6
Thrift	13.3	11.7	12.4	9.5	12.8
Credit union	1.9	2.2	2.5	2.7	2.6
<i>Mortgage companies</i>					
Independent	26.1	24.5	24.1	26.9	20.6
Owned by bank	30.7	28.0	28.0	31.2	30.6
Owned by holding company	8.8	7.9	2.0	1.8	11.0
Owned by thrift or credit union	6.8	7.5	8.7	7.6	3.9
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
 <i>Total number of applications</i>					
Subprime lenders	11,335	15,262	19,898	15,738	17,903
Manufactured home lenders	5,264	5,155	5,173	4,239	1,632
All others	126,370	146,858	162,008	181,286	203,479

Notes:

Figures report share of applications received in Washington and Baltimore MSAs.

Source: FFIEC (1999-2003).

Table 2. Industrial Segmentation, Conventional Home Improvement Market.

	(a) Subprime institutions.				
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	0.0	0.0	0.0	0.0	0.0
Bank (FRB)	0.2	0.1	0.0	1.2	1.3
Bank (OCC)	9.5	14.4	25.2	46.0	34.8
Thrift	5.6	20.7	10.0	1.7	1.7
Credit union	0.0	0.0	0.0	0.0	0.0
<i>Mortgage companies</i>					
Independent	20.6	9.4	8.5	48.5	55.0
Owned by bank	55.5	53.2	51.3	0.9	7.1
Owned by holding company	8.6	2.2	5.0	1.8	0.2
Owned by thrift or credit union	0.0	0.0	0.0	0.0	0.0
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
 (b) All others, excluding manufactured home lenders.					
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	6.0	6.4	6.4	6.2	9.4
Bank (FRB)	31.6	30.5	27.2	25.0	23.8
Bank (OCC)	16.7	20.2	24.5	30.9	23.5
Thrift	27.1	20.0	19.6	20.9	19.5
Credit union	16.6	19.2	20.0	15.5	20.1
<i>Mortgage companies</i>					
Independent	1.4	1.3	1.5	0.6	2.8
Owned by bank	0.6	1.6	0.6	0.5	0.1
Owned by holding company	0.0	0.8	0.1	0.0	0.2
Owned by thrift or credit union	0.0	0.0	0.2	0.4	0.6
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
 <i>Total number of applications</i>					
Subprime lenders	6,484	11,802	11,376	11,319	11,031
Manufactured home lenders	3,179	3,886	2,893	1,379	10
All others	31,466	30,387	31,632	31,429	24,664

Notes:

Figures report share of applications received in Washington and Baltimore MSAs.

Source: FFIEC (1999-2003).

The third trend hints at more subtle changes within these categories. Most notably, commercial banks played an increasing role in the subprime boom of the late 1990s. Institutions supervised by the OCC, for example, accounted for less than one percent of all subprime home purchase activity in 1998, 9.5 percent of home improvement applications, and 5.6 percent of the refinance market. By 2001, OCC-regulated banks attracted almost a fifth of subprime business in the refinance segment, more than a quarter of purchase loans, and an astonishing 46 percent of home improvement applications. Part of this shift reflects new lines of business, but much of it also stems from the growing interest of large banks in acquiring profitable subprime and predatory lenders.¹²

The net effect has been a wholesale institutional realignment of subprime specialization. There is still a broad division between purchase requests and the greater penetration of subprime capital in the renovation and refinance markets, but institutional channels have changed quite rapidly. Subprime activity in the purchase market flowed mostly through independent mortgage companies in 1998 (78 percent) although local thrifts also played a role; within a few years independents had lost substantial ground to commercial banks and mortgage

¹² The highest-profile illustrations of this trend include Citigroup's acquisition of Associates First Capital in 2000, and HSBC's acquisition of Household International in 2002. Associates was regarded as perhaps the nation's largest predatory lender, and Citigroup's acquisition immediately presented a high-profile target for organizing and regulatory challenges. The acquisition of Household, a large consumer finance and subprime lender, accounted for more than half of the increase in pre-tax profit posted by HSBC for 2003 (Timmons, 2004).

company subsidiaries of banks. The smaller home improvement market has been more volatile, with a decisive shift away from mortgage company subsidiaries to commercial banks as independent (and comparatively lightly regulated) mortgage companies regained a majority of the market. The refinance segment, with its repeated and unprecedented booms during this period of low interest rates, remained dominated by nondepository mortgage firms (Table 3). Mortgage subsidiaries of banks and holding companies, however, have overtaken independent firms. A substantial fraction of the subprime market penetration in the region's minority and lower-middle class neighborhoods is attributable to the subsidiaries of depository institutions (Figure 3).

Table 3. Industrial Segmentation, Conventional Refinance Market.

(a) Subprime institutions.					
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	0.0	0.3	1.1	0.7	1.0
Bank (FRB)	0.6	0.7	0.0	0.2	0.3
Bank (OCC)	5.6	5.5	11.0	18.5	10.9
Thrift	4.3	5.7	7.2	3.8	2.0
Credit union	0.0	0.0	0.0	0.0	0.0
<i>Mortgage companies</i>					
Independent	68.6	58.8	53.4	57.9	66.9
Owned by bank	7.3	18.6	17.4	10.1	9.5
Owned by holding company	13.6	10.2	9.4	8.2	8.1
Owned by thrift or credit union	0.1	0.3	0.6	0.7	1.4
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
(b) All others, excluding manufactured home lenders.					
	1998	1999	2000	2001	2002
<i>Depositories</i>					
Bank (FDIC)	3.0	2.3	2.6	2.4	2.8
Bank (FRB)	5.2	7.6	7.6	4.2	3.0
Bank (OCC)	10.2	17.6	29.4	13.7	11.0
Thrift	16.6	15.0	14.9	11.6	16.3
Credit union	4.2	4.2	4.1	6.4	6.1
<i>Mortgage companies</i>					
Independent	18.6	17.4	15.1	22.7	17.4
Owned by bank	31.2	26.1	19.2	29.8	28.1
Owned by holding company	4.9	4.4	1.7	2.0	12.0
Owned by thrift or credit union	6.1	5.5	5.5	7.1	3.4
<i>Totals</i>	100.0	100.0	100.0	100.0	100.0
<i>Total number of applications</i>					
Subprime lenders	74,884	76,968	59,972	83,819	117,328
Manufactured home lenders	4,082	3,095	2,032	2,746	231
All others	214,587	145,741	74,113	290,070	460,737

Notes:

Figures report share of applications received in Washington and Baltimore MSAs.

Source: FFIEC (1999,2003).

These trends underscore the importance of understanding the institutional channels through which ever larger streams of housing capital flow. From the beginning of 2001 through March 2002, for instance, cash-out refinancing effectively liquefied \$132 billion of home equity nationwide, and total home mortgage debt outstanding increased by \$616 billion (Canner, Dynan, and Passmore, 2002, p. 479). In most cases, consumers took cash-out refis to pay off credit cards, other debts, or to finance other consumption priorities. But these enormous flows also provided lucrative opportunities for lenders, brokers, appraisers, and investors ~ particularly in the comparatively unregulated arena of non-depository mortgage banking. In many respects, then, the expansion of subprime activity in the refinance and home improvement markets has created a contemporary parallel to the controversial role of Federal Housing Administration (FHA) insurance. After amendments in the late 1960s changed FHA's mission to serve lower-income, first-time buyers, the specific provisions of default insurance created perverse incentives for lenders to make unsound home-purchase loans and then pursue rapid foreclosure (Wachter, 1980). Many analysts began to see high rates of FHA-insured lending in the purchase market as an indicator of irresponsible lending (Bradford and Rubinowitz, 1975). Controversy persists over abuses of FHA-insured lending (Bradford, 1998), and over the appropriate way of interpreting the geographical

concentration of FHA market share in minority and lower-middle class neighborhoods (Figure 6). These debates have been complicated by the rapid proliferation of high-risk subsidiaries in the 1990s, replacing the old dichotomy between conventional and FHA lending with a tripartate stratification of conventional prime, FHA-insured, and conventional subprime credit. For minority and working-class communities, the results have been mixed and often contradictory. The expansion of the subprime sector does not seem to have altered the simplest aspects of credit rationing ~ the clustering of high denial rates in those places where conventional prime banks have given way to mortgage firms specializing in B-and-C lending or FHA insured products (Figure 5). To be sure, these housing submarkets are risky, because a greater proportion of hopeful borrowers are likely to have employment histories or credit records that will arouse underwriters' concerns (Figure 6). But credit history is far from an objective, unproblematic measure.¹³ In any event, subprime lenders have made quite aggressive moves even into quite risky markets, encouraged by deregulation, demonstration effects of public policies, and sophisticated target marketing databases. The secondary market has also been a key factor: most of the subprime loans made by firms operating in minority and working-class neighborhoods are sold almost immediately to investors (Figure 7).

¹³ Extreme caution is required when evaluating the credit denial map (which seems to blame borrowers) alongside the subprime market penetration map (which suggests at least some responsibility of lenders). The credit denial map can be only regarded as a map of borrower 'deficiencies' if we place full faith in denial codes (which are optional) cited by lenders who have clear incentives to cite a legitimate factor as a means of concealing disparate treatment or disparate impact discrimination. Marsico (1999), in a study of New York lending patterns, noted that "lenders appear to be using several criteria for evaluating loan applications that have a disparate impact on Latinos, African Americans, or both. The HMDA permits, but does not require, lenders to report the reasons they denied a loan. A lender can report eight specific reasons for denying a loan. If a lender denies loans to minorities at a disproportionately higher rate than whites based on the failure to satisfy a particular criterion, that criterion has a disparate impact on minorities. In order to pass scrutiny under the fair lending laws, the lender would have to justify its use of this criterion on the basis that the criterion had a legitimate business purpose and that there were no alternative criteria that would serve the same business purpose but would not have a disparate impact." (pp. 522-523). Marsico's (1999) empirical evidence points to disparate impacts for African Americans and Latinos on the basis of credit history, but he did not examine the spatial dimensions of this impact. Additionally, the spatial aspects of cultural affinity theories (Hunter and Walker, 1995) and other explanations for discrimination will tend to reinforce the kinds of patterns shown in Figure 6. If white applicants in white, wealthy neighborhoods are more likely to be coached on how to clean up a blemished credit report, we would expect far fewer bad-credit denial in these places.

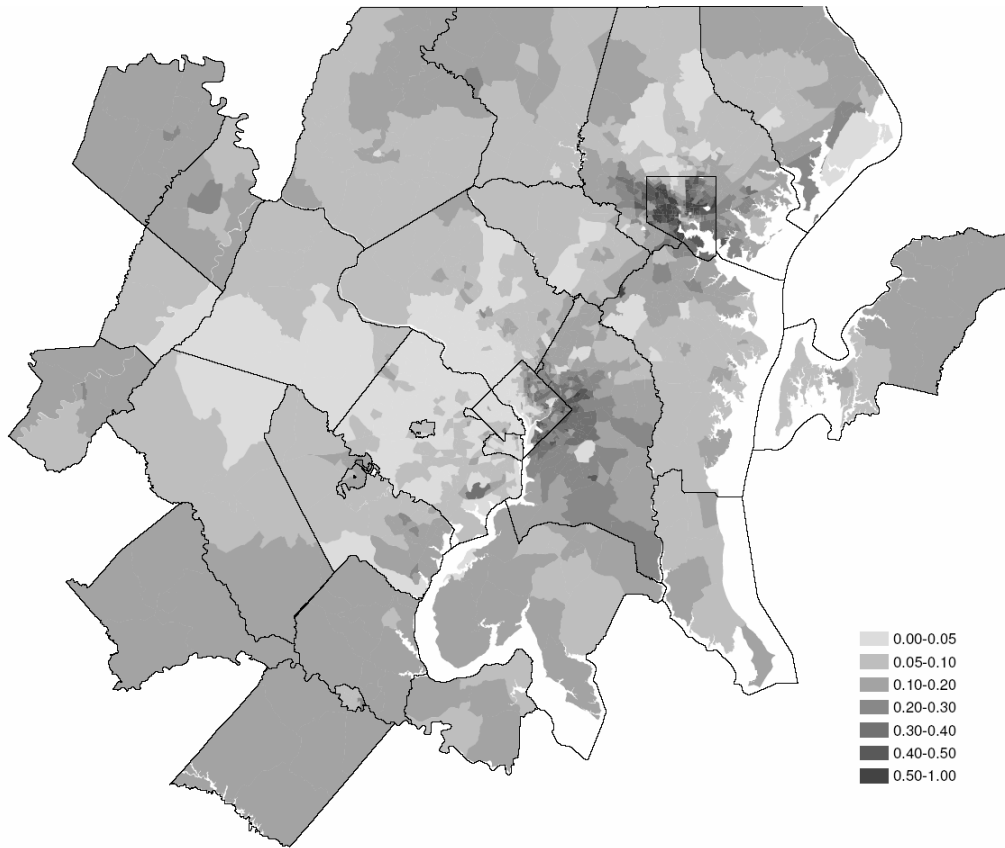


Figure 2. Subprime share of conventional refinance originations, 1998-2002. Source: *FFIEC (1999-2003)*.

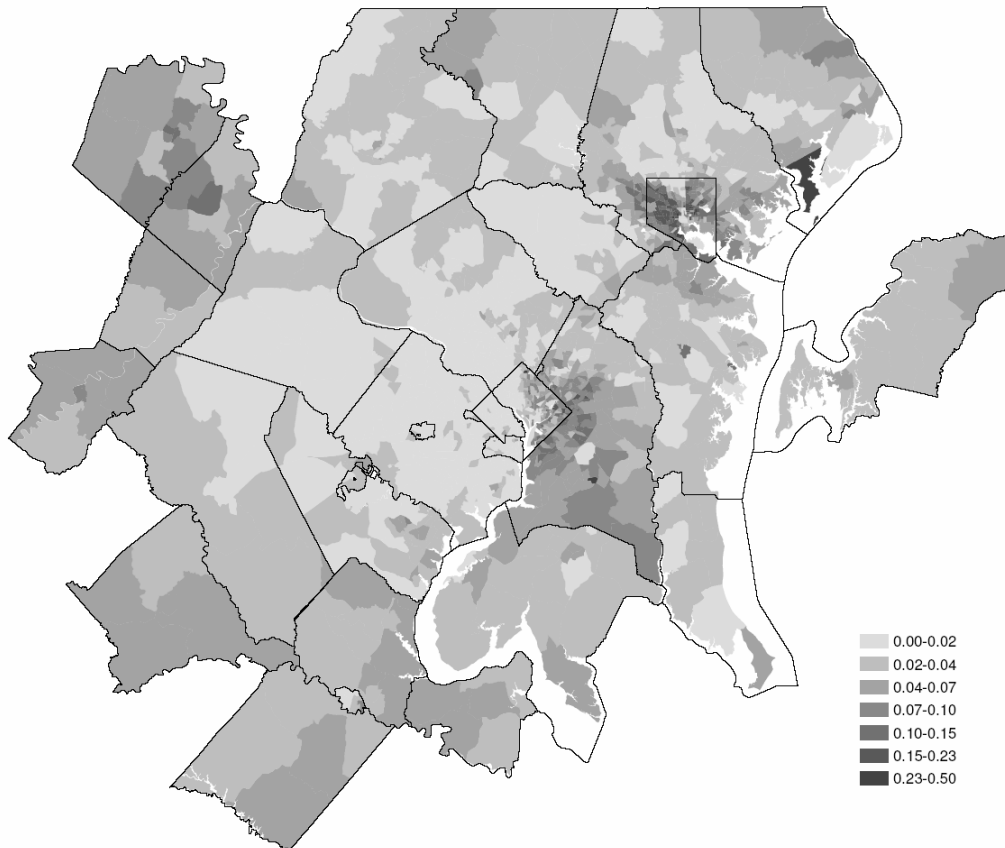


Figure 3. Conventional refinance originations by subprime divisions of banks, thrifts, and bank holding companies, as share of all conventional refinance originations, 1998-2002. Source: *FFIEC (1999-2003)*.

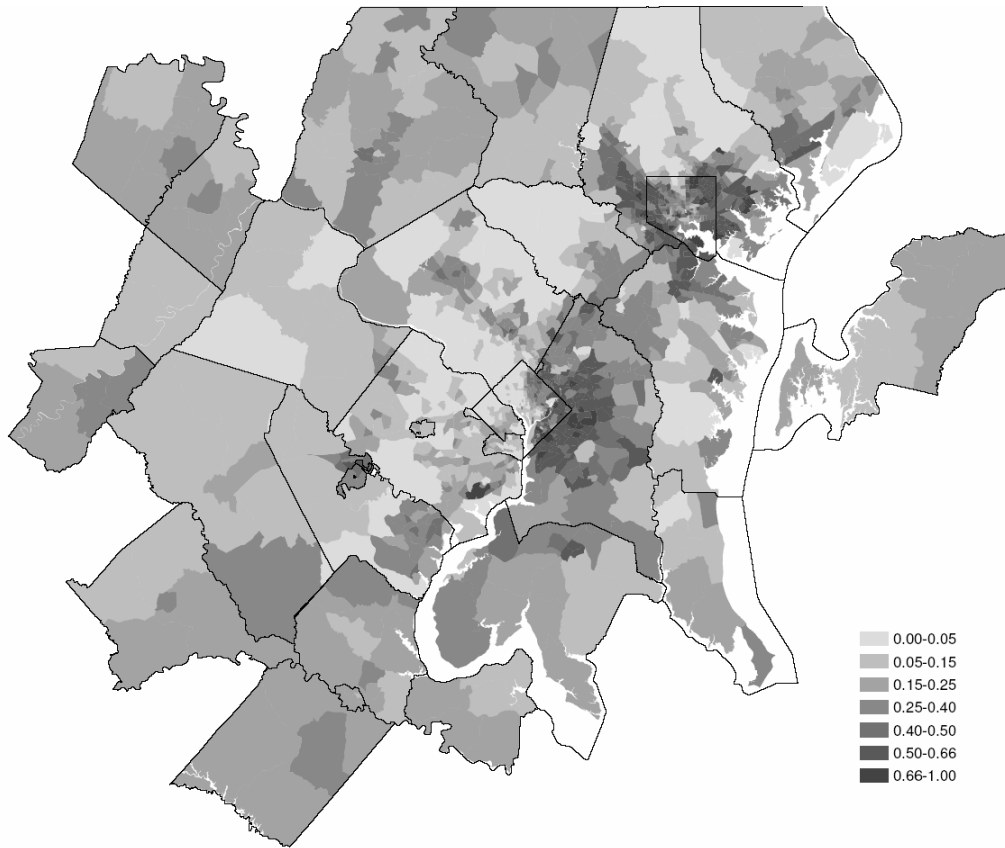


Figure 4. Share of home purchase originations insured by FHA, 1998-2002. *Source: FFIEC (1999-2003).*

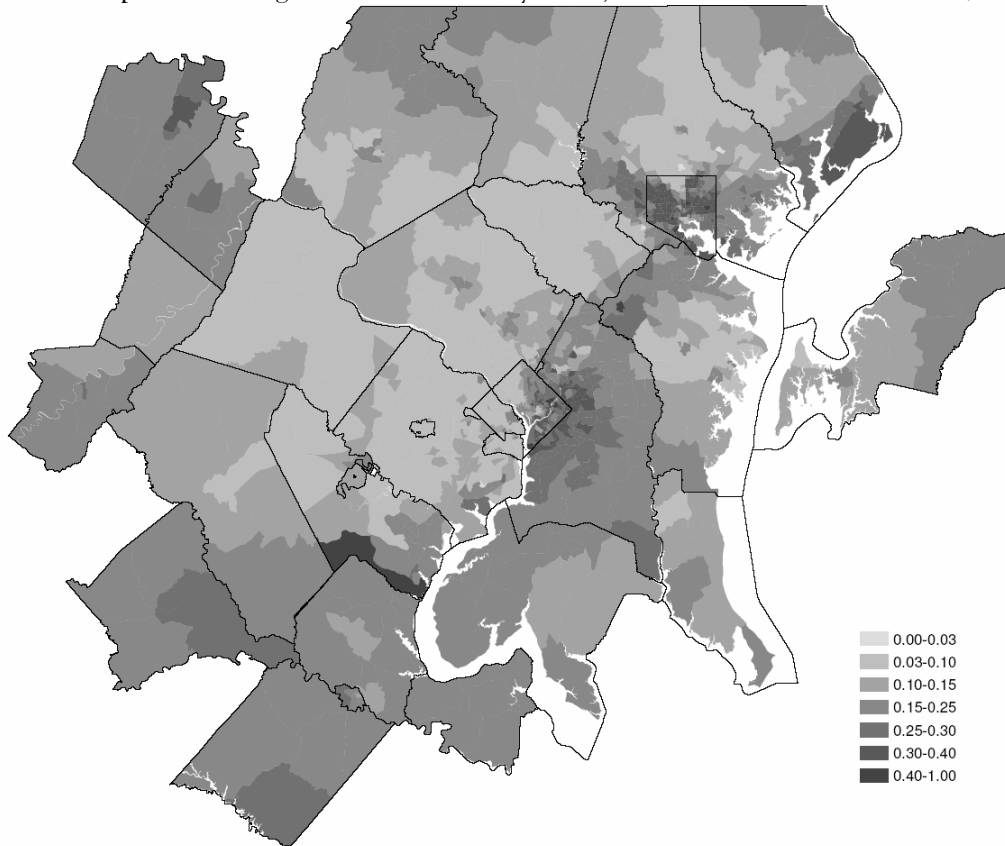


Figure 5. Overall denial rate, 1998-2002. Share of all single-family applications for purchase, renovation, or refinance denied by institution. *Source: FFIEC (1999-2003).*

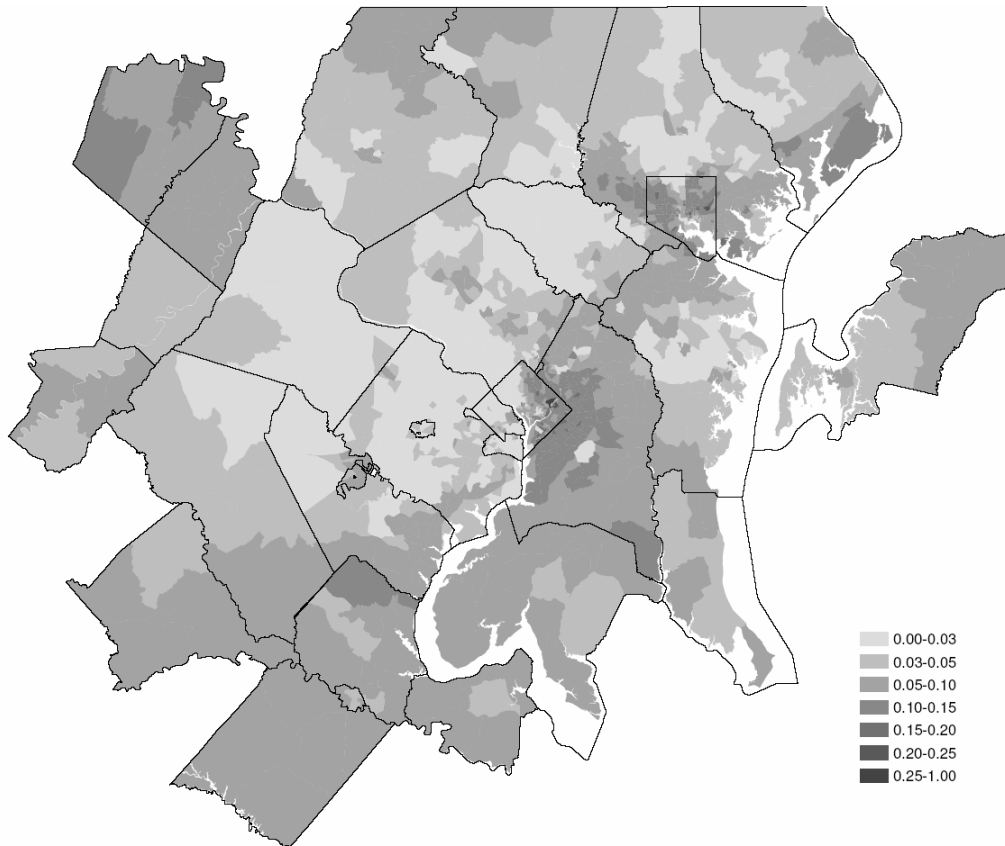


Figure 6. Share of all applications denied and cited for credit history, 1998-2002. *Source: FFIEC (1999-2003).*

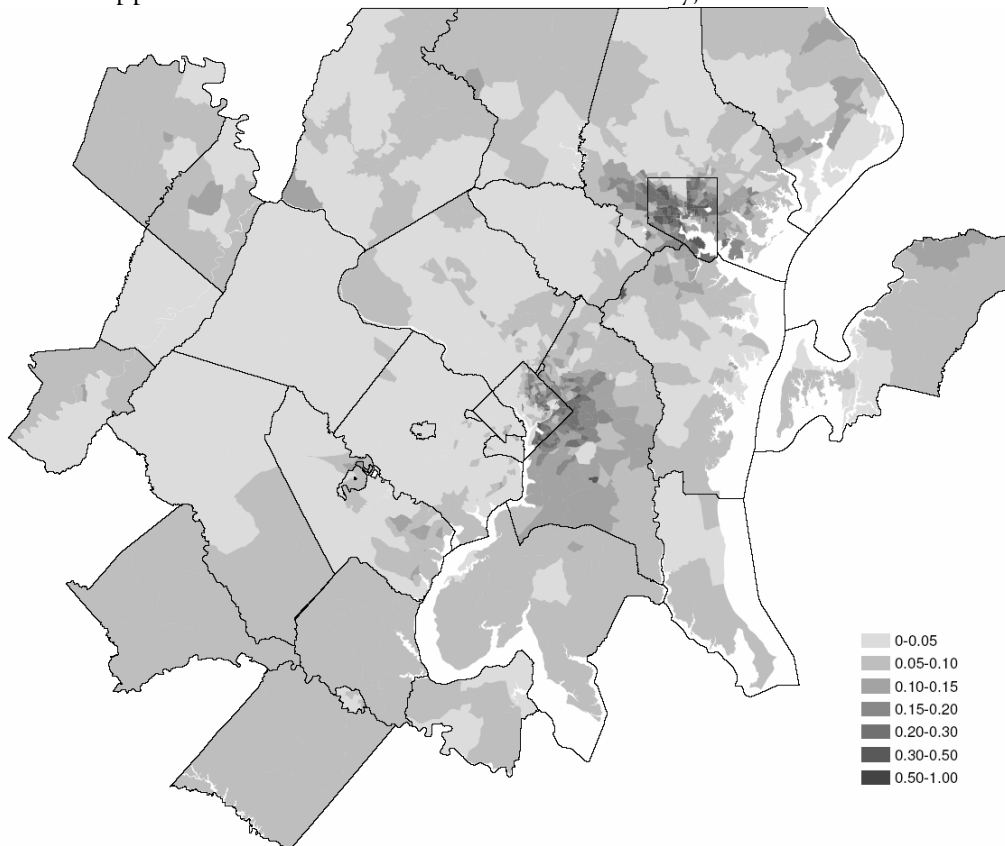


Figure 7. Conventional refinance loans originated and sold by subprime lenders, as share of all conventional refinance originations, 1998-2002. *Source: FFIEC (1999-2003).*

Modeling Segmentation

These simple tables and maps are illuminating, but they cannot distinguish between the many characteristics of lenders and the circumstances of individual homeowners. A multivariate approach is required for a rigorous evaluation of changes in the institutional aspects of class-monopoly rent in the mortgage market. Let's consider the demand side first. Let p be the probability that an individual loan application is filed at an institution specializing in subprime lines of business. A standard approach in the urban and housing economics literature involves a model of borrowers' choices, as expressed in the correlation between p and a set of household finances (\mathbf{F}'), loan terms (\mathbf{L}'), and demographic characteristics (\mathbf{D}'):

$$\ln \left[\frac{P_{subprime}}{1 - P_{subprime}} \right] = \beta_0 + \beta_F \mathbf{F}'_i + \beta_L \mathbf{L}'_i + \beta_D \mathbf{D}'_i + \varepsilon_i \quad [1]$$

As in the extensive literature on loan rejection and credit rationing, the interpretation of the most interesting coefficients from this type of model ~ for instance, the role of race/ethnicity in market segmentation ~ is deeply influenced by omitted-variable bias. The mortgage disclosure files provide no direct information on loan terms offered by lenders, or on applicant credit histories, liquid assets, employment history, and other crucial considerations used by lenders to evaluate risk, profitability, performance, and salability. Thus if we observe a positive, significant coefficient for African Americans, we cannot determine *why*: African Americans may have fewer assets and poorer credit histories, and therefore they may choose lenders who market their leniency on these terms.¹⁴ Yet since the dependent variable is loan segmentation (and not loan rejection) we can use the action taken on the loan as a right-hand side, reduced-form indicator of the underwriter's evaluation of a particular file. If we code these actions as right-hand side predictors (\mathbf{A}'), the resulting model captures segmentation effects that persist after accounting for variations in applicant "quality" *as seen by underwriters and loan officers*:

$$\ln \left[\frac{P_{subprime}}{1 - P_{subprime}} \right] = \beta_0 + \beta_F \mathbf{F}'_i + \beta_L \mathbf{L}'_i + \beta_D \mathbf{D}'_i + \beta_A \mathbf{A}'_i + \varepsilon_i \quad [2]$$

This approach presents a stark contrast to the accept/reject models which have dominated the discrimination and redlining debates (e.g., Carr and Megbolugbe, 1993; Munnell et al., 1992, 1996; Ross and Yinger, 2002; Schill and Wachter, 1993). Placing the loan outcome indicators on the right hand side severs the link between the object of study and the problem of omitted variable bias; instead, we put full trust in the decisions of underwriters and lenders. The \mathbf{A} vector captures as much of the omitted variable bias (as well as partial observability and self-selection biases) as possible (see Rachlis and Yezer, 1993).¹⁵ The \mathbf{A} vector includes the evaluations of lenders who decide to approve or reject after considering individual and neighborhood risk factors, as well as the profitability of the transaction; it also incorporates the choices made by applicants who withdraw or abandon their files after having second thoughts. If a β coefficient for African Americans remains positive and significant despite the addition of \mathbf{A} , it provides strong evidence of some kind of racial targeting that cannot be attributed to borrower choice or credit quality.

¹⁴ Among the most blatant appeals to poor-credit applicants was used by a partner institution to Superior Bank, one of the banks targeting African-American neighborhoods that is profiled later in this article. A marketing flier showed an image of a trash can, with a tag line that borrowers regarded by other banks as "refuse, garbage, riffraff, and drivel" were just what the company wanted (Day, 2001).

¹⁵ Rachlis and Yezer's (1993) detailed discussion of the econometric biases in lending research still applies to the field a decade later. Our approach helps to control for some of these biases, but Eq. [2] nevertheless remains vulnerable to self-selection bias. We attempt to control for this problem later in this paper.

Now consider an alternative, supply-side view of the market. The probability that any given lender will specialize in subprime business is a function of its overall level of profitability and its market share (\mathbf{M}'), its type of charter and regulatory supervision (\mathbf{T}'), the overall credit quality of the applicants it can attract (\mathbf{Q}'), and its integration into lucrative secondary-market sales conduits (\mathbf{S}'):

$$\ln \left[\frac{P_{subprime}}{1 - P_{subprime}} \right] = \beta_0 + \beta_M \mathbf{M}'_i + \beta_T \mathbf{T}'_i + \beta_Q \mathbf{Q}'_i + \beta_S \mathbf{S}'_i + \varepsilon_i$$

[3]

In this specification, coefficients for the \mathbf{M} and \mathbf{S} vectors are particularly valuable to assess how Harvey's (1974, 1978, 1985) circuits of finance capital in Baltimore have been reshaped by a generation of industrial, political, and technological change. We estimated these supply and demand equations for all usable loan applications backed by properties in the study area between 1998 and 2002.¹⁶ Our estimates incorporate as many relevant variables as possible, given the particular and limited view that can be gained from the HMDA files (see Tables 4 and 5).¹⁷ Most of the applicant variables follow the established conventions of the mortgage lending literature (e.g., Harrison, 2000; Holloway, 1998; Ross and Yinger, 2002; Schill and Wachter, 1993), but several specialized measures capture the flows of capital that are central to our analysis. Binary variables are coded for loans that are originated and sold in the same calendar year to one of the GSEs (Fannie Mae or Freddie Mac), to a bank, or to some other type of secondary market investor. On the supply side our variables distinguish among various market niches, such as predominantly refi lenders, or firms specializing in very high-risk segments where denials or withdrawals are more common, or companies geared to underserved markets. Central to our engagement with Harvey's work are the variables for market share, the ratio between local and national market share, and the secondary market indicators.

Results

Maximum likelihood estimates suggest robust, stable coefficients for both demand- and supply-side specifications (Tables 4 and 5). Measures of overall fit exceed those typically reported in accept/reject studies (by a considerable margin in the case of the supply-side model) (Nagelkerke, 1991). The inclusion of a lengthy (but by no means comprehensive) array of predictors helps to reduce the risks of omitted-variable bias, but there are also encouraging results from multicollinearity tests.¹⁸ A second specification for the demand-side model corrects for the few problems that do persist, with only minor effects on most of the other coefficients (compare Models 1 and 2 in Table 4).

¹⁶ Pre-processing involves screening out applications with missing locational information, typically a tiny percentage of all records (none in 1998 and 1999, 31 in 2000, 4 in 2001, and 16 in 2002). Additionally, the 2002 HMDA included duplicate submissions by two divisions of one large subprime lender (Conseco) (Scheessele, 2003). Eliminating these double-counted records in our study area required the deletion of 341 home purchase applications, 173 renovation applications, and 230 refinance applications. Finally, we dropped records for one mortgage company that coded no loan purpose for two dozen applications received in 2000, and we also omitted the handful of records for loan amounts exceeding \$10,000,000.

¹⁷ As one illustration of the severity of these restrictions, note that our supply variables include no measures of return on investment or other aspects of profitability. Information of this sort is available for most banks and other depository institutions, but is much more difficult to document for independent mortgage companies. In the case of assets, moreover, the variable has fundamentally incompatible meanings for different kinds of firms: banks report all assets (not just mortgages), while most independent mortgage originators have negligible assets due to their pass-through role.

¹⁸ Using the criteria outlined in Menard (2002), only two variables in Model 1 in Table 6 show evidence of significant multicollinearity: income and income squared post tolerance values below 0.20, "a cause for concern" (Menard, 2002, p. 76). All other tolerances exceed 0.5, and fifteen of the twenty-seven exceed the comfortable threshold of 0.80. Given the theoretical and practical importance of income, we present a fully-specified demand model as well as one without the collinear variables. For the supply-side model (Table 7) none of the predictors exhibit problematic tolerances, and twelve of twenty-two exceed 0.70.

Table 4. Demand-Side Models of Subprime Segmentation.

Variable	Model 1		Model 2	
	Parameter	Odds	Parameter	Odds
	Estimate	Ratio ¹	Estimate	Ratio ¹
Intercept	-2.3022		-2.9869	
Income (\$,000)	-0.00623	0.32		
Income squared	0.00000603	2.18		
Payment ratio	-0.00128	0.97	0.00696	1.22
Ratio squared	0.000000861	1.01	-0.00000656	0.46
Loan exceeds GSE limit	-0.281	0.76	-0.848	0.43
FHA-insured	-2.021	0.13	-1.970	0.14
Owner-occupancy	0.027	1.03	0.120	1.13
Home improvement ²	0.345	1.41	0.445	1.56
Refinance	0.747	2.11	0.755	2.13
Year 1999 ³	0.194	1.21	0.188	1.21
Year 2000	0.273	1.31	0.251	1.29
Year 2001	-0.209	0.81	-0.259	0.77
Year 2002	-0.210	0.81	-0.267	0.77
Native American ⁴	0.194	1.21	0.179	1.20
Asian or Pacific Islander	-0.520	0.59	-0.569	0.57
African American	0.699	2.01	0.729	2.07
Hispanic	-0.001 *	1.00	0.017 *	1.02
Other race/ethnicity	0.624	1.87	0.609	1.84
Race unreported	0.929	2.53	0.933	2.54
Corporate applicant	1.502	4.49	1.453	4.27
Traditional white family couple	-0.415	0.66	-0.504	0.60
Female applicant	0.013	1.01	0.071	1.07
Edit failure	0.017	1.02	-0.013	0.99
Denied ⁵	1.672	5.32	1.757	5.80
Declined by applicant	1.337	3.81	1.360	3.90
Withdrawn	1.883	6.57	1.902	6.70
Closed as incomplete	1.268	3.55	1.287	3.62
Originated and sold to GSE	-2.885	0.06	-2.914	0.05
Originated and sold to bank	-0.298	0.74	-0.317	0.73
Originated and sold to affiliate	0.053	1.05	0.038	1.04
Originated and sold to other purchaser	0.949	2.58	0.949	2.58
Number of observations	2,789,254		2,789,254	
Nagelkerke (1991) Pseudo-R ²	0.43		0.42	
Percent correctly classified	86.6		86.2	

*Coefficient not significant at P<0.05. All other coefficients are significant at P<0.01.

¹ Entries for continuous variables report the change in odds with a one standard deviation increase.

² Reference category for loan purpose is home purchase applications.

³ Reference category for year is 1998.

⁴ Reference category for race/ethnic and gender variables is white male primary applicants.

⁵ Reference category for action taken is approved and originated, but not sold in the same calendar year.

The demand models follow the broad outlines of the conservative and industry perspective on high-risk lending. As it claims, the industry is oriented towards the credit needs of lower-income borrowers: a one-standard deviation increase in applicant income reduces the chance that a borrower will choose a subprime lender by two-thirds. Similarly, the industry focuses on borrowers who are more difficult to underwrite, or who encounter other difficulties that lead to second-thought withdrawals or incomplete files. Compared with applicants who sail through the process and obtain loans, those who are denied are more than five times as likely to have approached a subprime lender; the ratio is even higher for those who withdraw their requests. Given the willingness of subprime lenders to serve higher-risk borrowers, it is not surprising to see them focusing on those parts of the business where lower loan-to-value ratios provide a cushion against default (note the high odds ratios for the home improvement and refinance markets).

Even after accepting this conservative interpretation, however, several results point to the role of capital investment and supply-side processes. The disproportionate segmentation of racial and ethnic minorities provides indirect evidence of targeting ~ either on the basis of individual race, neighborhood racial composition, or some combination of the two. African Americans are more than twice as likely to be in the subprime market compared with whites at the same income level and debt burden; and since loans rejected or withdrawn because of credit history, employment stability, and other concerns are factored in as control variables, it becomes difficult to blame the racial segmentation on applicant risk factors. Segmentation is even stronger for applicants with unreported

race/ethnicity; subprime lenders tend to make heavy use of marketing tactics that slip through loopholes of the federal rules requiring lenders to ask people to self-identify for fair lending enforcement purposes (Huck, 2001; Wyly and Holloway, 2002). The overwhelming reliance of corporate applicants on the subprime sector is also cause for concern. These applicants constitute a tiny fraction of the regional market (less than one half of one percent), but anecdotal evidence from other markets has uncovered sham nonprofit corporations established to qualify for various government subsidies and then to trick unsuspecting people into buying run-down homes at inflated prices (Pristin, 2000).

Table 5. Supply-Side Models of Subprime Segmentation.

Variable	Model 1		Model 2	
	Parameter	Odds	Parameter	Odds
	Estimate	Ratio ¹	Estimate	Ratio ¹
Intercept	-7.1103		-7.1285	
Lender market share	0.6156	2.15	0.6145	2.14
Ratio of local to national market share	-0.1439	0.20	-0.1441	0.19
Depository institution ²	-3.5531	0.03	-3.5416	0.03
Mortgage company owned by depository	0.6794	1.97	0.685	1.98
Lender denial rate	0.0392	1.92	0.0375	1.86
Declination rate	0.0506	1.57	0.0498	1.56
Withdrawal rate	0.0763	2.58	0.0745	2.52
Closed as incomplete rate	0.016	1.06	0.015	1.06
Owner-occupied share	0.0216	1.11	0.0217	1.11
FHA rate	-0.0864	0.29	-0.0854	0.29
Jumbo share	-0.0349	0.74	-0.0337	0.75
African American share	0.1378	4.65	0.1368	4.60
Hispanic share	0.0407	1.12	0.0409	1.12
Other share	0.0837	1.34	0.0824	1.33
Lender race non-reporting rate	0.0332	2.53	0.032	2.45
Lender edit failure rate	0.0179	1.82	0.0178	1.82
Share of originations sold to GSEs	-8.4188	<0.001	-8.3868	<0.001
Share of originations sold to banks	-2.0825	0.63	-2.0757	0.63
Share of originations sold to affiliates	0.5067	1.13	0.5078	1.13
Share of originations sold to other purchaser	0.1499	1.08	0.1406	1.07
Home improvement ³	-0.0204 *	0.98	-0.065	0.94
Refinance	0.0255	1.03	-0.078	0.92
Year 1999 ⁴	0.0229 *	1.02	0.00374 *	1.00
Year 2000	0.191	1.21	0.1652	1.18
Year 2001	0.3234	1.38	0.35	1.42
Year 2002	0.5233	1.69	0.5488	1.73
Applicant instrumental variable			0.6006	1.15
Number of observations	2,789,254		2,789,254	
Nagelkerke (1991) Pseudo-R ²	0.87		0.87	
Percent correctly classified	98.7		98.7	

*Coefficient not significant at $P < 0.05$. All other coefficients are significant at $P < 0.01$.

¹ Entries for continuous variables report the change in odds with a one standard deviation increase.

² Reference category for lender type is independent mortgage companies.

³ Reference category for loan purpose is home purchase applications.

⁴ Reference category for year is 1998.

The Secondary Market, Circuits of Capital, and Lender Specialization

Controlling for the varied characteristics of those wishing to *borrow* capital allows us to shift the focus to those who want to *lend* it. Several results shed light on the ways that contemporary practices in the banking industry and the financial markets perpetuate stratification of capital flows in the city. In the demand model, the secondary market indicators confirm that lenders' decisions and relations with investors are crucial in understanding segmentation. Loans sold in the same calendar year to one of the GSEs are extremely unlikely at subprime lenders, an unsurprising result in light of the intense public scrutiny and policy debates in recent years over the roles and responsibilities of Fannie Mae and Freddie Mac (see, e.g., Apgar et al., 2004; Fannie Mae,

2003; Freddie Mac, 2003; and summaries of testimony by several regulators in Butera and Andrews, 2000).¹⁹ The subprime sector is much more closely tied to loan sales that no longer fit the old, traditional categories identified in the data: compared with loans originated and held (at least temporarily) by the lender, loans sold to some “other purchaser” are 2.6 times more likely to be in the subprime segment. Although this ambiguous category can include life insurance companies and other investors, the B-and-C market is increasingly governed by the activities of special purpose vehicles (SPVs), which are established solely to hold loan pools for a short time in order to break the chain of legal liability. SPVs then assign the loans to a trust, which in turn issues securities for sale on the financial markets (Eggert, 2003, 2004; Engel and McCoy, 2004).²⁰

The supply model offers the most colorful portrait of the behavior of finance capital (see Table 5). We estimated two versions: one based simply on Eq. [2], and another that includes an instrumental variable to predict the likelihood that an individual applicant will choose to apply at a subprime institution.²¹ The close correspondence of the coefficients for these two models (note, for instance, the African American share parameter of 4.60 versus 4.65) corroborates the role of independent, supply-side processes that cannot be explained simply as a response to consumer demand. Institutional strategy remains crucial even after considering individual qualifications, needs, and choices. The subprime sector has come to be dominated by large, non-local mortgage companies, many of them bank subsidiaries, that specialize heavily in the African American market. These effects are robust and substantial. Approaching a lender with a national market share that is one standard deviation above the mean doubles the chance of ending up at a subprime institution, all else constant; going to a more locally-oriented company, *reduces* the odds by five times. Firms that are one standard deviation above the average in terms of African American specialization are more than four times as likely to be subprime. Compared with independent mortgage companies, those owned by banks are almost twice as likely to focus on B-and-C lending. All of these results are consistent with the idea that stratified neighborhood credit markets are integrally tied to the conditions of capital investment and financial services restructuring, and to the creation of a specialized institutional structure to target particular groups of homeowners and homebuyers.

Mapping the Spatiality of Subprime Capital

These model results illuminate the complex networks of capital flows that shape contemporary relations of class-monopoly rent. But do these relations imply that spatial patterns of the sort identified by Harvey a generation ago are nothing more than incidental expressions of fundamentally economic processes? Are the models presented in Tables 4 and 5 sufficient to understand the dynamics of subprime capital, or do space and place matter? We analyze these questions in three complementary ways; each builds on the supply- and demand-side models, thereby controlling for all characteristics of borrowers and lenders that can be observed through the disclosure records. If spatial variations persist after accounting for these controls, then our central concern is to determine whether the patterns make any sense from an urban-regional geographic perspective: if segmentation is purely economic, then we should find nothing more than minor, random, and idiosyncratic spatial variations.

¹⁹ It is important to note, however, that the magnitude of this coefficient estimate is not a sign of spurious problems driving the entire equation and artificially inflating the model fit diagnostics. Models re-estimated without the secondary market sales indicators yield similar coefficient estimates for most of the other variables (the notable exception involves a reduction of the importance of market share) and nearly identical fit measures (e.g., Nagelkerke indices of 0.84 versus 0.87 for both models reported in Table 5).

²⁰ “In addition, once loans are securitized, under the holder-in-due-course rule, borrowers typically cannot defend nonpayment on the grounds that the lenders engaged in unlawful activity related to the loans, such as committing certain types of fraud on borrowers. ... This has the effect of increasing the value of the loans upon securitization.” Engel and McCoy, 2002, p. 1274, note 67.

²¹ This approach has been used in the discrimination literature as one way of estimating applicant credit risk (see Abariotes et al., 1993, and Holloway, 1998). The applicant instrument we use is calculated for each borrower using the coefficients from Model 1 in Table 4. For the entire dataset, the applicant instrument has a mean of 0.21 and a standard deviation of 0.23. The instrument averages 0.46 among applicants at subprime lenders, and 0.14 for all other institutions.

The first approach is simple: adding a vector of locational dummies to test for statistically significant differences across thirty-two units of local government in the region.²² We use the first demand specification (given the theoretical importance of applicant income), and both versions of the supply model. To facilitate interpretation, odds ratios are replaced with calculations of the probability that a typical “reference applicant” will end up at a subprime lender; we then compare the experience of this applicant in each city or county across the region with an otherwise identical borrower in Washington, D.C.²³

Table 6. County-Level Segmentation.

	<i>Subprime probability for reference applicant</i>		
	<i>Demand Model</i>	<i>Supply Model 1</i>	<i>Supply Model 2</i>
Washington, DC	18.4	18.0	18.5
Anne Arundel County	25.5	22.6	23.6
Baltimore County	28.2	21.9	22.7
Calvert County	23.8	21.1	22.1
Carroll County	24.7	21.4	22.6
Charles County	26.7	22.3	23.2
Frederick County	26.1	21.8	22.9
Harford County	27.9	23.7	24.7
Howard County	22.1	20.5	21.6
Montgomery County	20.0	19.2	20.3
Prince George's County	29.3	22.6	23.2
Queen Anne's County	26.7	24.1	25.2
Baltimore City	38.5	29.3	29.7
Arlington County	12.0	15.8	16.8
Clarke County	25.9	19.5	20.5
Culpeper County	37.0	28.7	29.8
Fairfax County	16.6	18.7	19.8
Fauquier County	27.3	25.3	26.6
King George County	38.0	30.5	31.5
Loudon County	16.9	18.4	19.5
Prince William County	24.8	21.7	22.6
Spotsylvania County	36.4	27.6	28.5
Stafford County	31.3	23.1	24.1
Warren County	35.7	22.2	23.0
Alexandria City	13.8	18.0	19.0
Fairfax City	16.6	18.2	19.3
Falls Church City	13.6	17.0	18.2
Fredericksburg City	33.5	29.2	30.1
Manassas City	27.2	25.0	26.0
Manassas Park City	35.1	25.4	26.4
Berkeley County	42.0	42.4	43.3
Jefferson County	32.0	32.4	33.3
Range	30.0	26.7	26.5
Mean	26.7	23.4	24.3
Standard Deviation	8.0	5.4	5.4

This approach reveals durable local variations in the regional landscape of housing markets and capital flows (Table 6). Each of the three models yields similar results, but we focus here on the most robust estimates of the

²² This regionalization corresponds to a county-level analysis in Maryland, Washington, D.C., and West Virginia; Virginia is unique by virtue of a legal framework granting certain independent cities full autonomy from their surrounding counties.

²³ For the demand side, we take as a reference applicant a person who wishes to buy a home for owner-occupancy in 2002, who has average income and debt load, and whose application is approved, originated, and held by the bank at least through the end of the year; we also assume that the race/ethnicity of this borrower is not reported. For the supply side, we consider that our applicant approaches a mortgage company subsidiary of a bank that sells only a tenth of its annual business to the GSEs, and is average in terms of market share, denial rate, and all other measures.

second supply model. A typical borrower faces the lowest chances of segmentation (between 17 and 20 percent) in Washington and its adjacent western and northwestern suburbs (in Maryland, Montgomery County, and on the Virginia side, Arlington, Alexandria, Fairfax City and County, Falls Church) as well as the more distant suburbs of Loudon County, Virginia. All of these areas encompass the region’s wealthiest neighborhoods, although the city of Washington is also of course marked by severe poverty in the Northeast and Southeast quadrants. An identical applicant faces much higher probabilities, by contrast, in the city of Baltimore, several modest middle-class areas woven into regional commuting networks on the southern crescent of the metropolitan area (Culpeper, Spotsylvania, and King George counties, Fredericksburg city), and the expanding ranks of modest subdivisions and mobile-home communities in the West Virginia Panhandle (Berkeley and Jefferson counties). These patterns clearly reflect the broad outlines of subprime market share when we ignore borrower and lender characteristics; and the pattern is by no means trivial or random. Mortgage capital has a clear spatiality that cannot be reduced to non-geographic elements of demand and supply.

The Neighborhood Scale

A sharper image appears if we consider the relative fit of demand and supply side explanations at the neighborhood scale. For each loan applicant in the region, we computed separate segmentation probabilities with the demand and supply side specifications (i.e., Model 1 in Tables 4 and 5). We then average the individual values by tract and compute an index, dividing the demand-implied estimate by the supply-based estimate. The index measures how well localized market outcomes can be explained in terms of the correspondence between borrower and lender characteristics.²⁴

The results are striking. Global estimates yield a precise match: for the entire population of 2.79 million applicants, the average probability estimates (21.02 percent) match within six millionths (i.e., the demand estimate is 0.0006 percent higher). But regional convergence hides substantial and meaningful variation at the tract level (Figure 7). In dozens of neighborhoods, low demand-supply ratios indicate that applicant characteristics can only explain half or three-quarters of the probabilities suggested by lending institution characteristics; in these places, it seems justified to conclude that the strategies of lenders, investors, and others on the supply side are more important than the presumed deficiencies of local homeowners and homebuyers. Conversely, high ratios in other neighborhoods are a sign that borrower profiles, on average, justify more subprime activity than is suggested by the characteristics of lenders. The geographies of these alternative paths are fascinating. High ratios (at least 1.25, and in several dozen cases 1.75 or more) spread across the elite and upper-middle-class districts of Georgetown, Arlington, Alexandria, Northwest D.C., to the northwest suburbs on the Maryland side of the Potomac, and west through Virginia’s Fairfax County into the growth corridors and horse-country subdivisions of Loudon County. In all of these areas, homeowners and homebuyers have characteristics that would seem to justify considerable subprime activity ~ much more than we expect on the basis of lender characteristics. Prime lenders are pursuing many borrowers who have the debt ratios or other risk factors of subprime applicants. On the other hand, broad sections of lower-middle-class and working-class neighborhoods across the region post unusually low index values ~

²⁴ Formally, our calculation for each tract is:

$$\frac{\sum_{i=1}^n \hat{p}_{d_i} / n}{\sum_{i=1}^n \hat{p}_{s_i} / n}$$

where the estimated demand (\hat{p}_d) and supply (\hat{p}_s) probabilities for applicant i are calculated as $e^{\beta_0 + \beta_x X}$ with X vectors as defined by Model 1 coefficients in Tables 4 and 5, and where n is the number of applicants in the census tract. To avoid the bias of small numbers, we restrict this calculation to census tracts where at least 100 applications are filed between 1998 and 2002.

a sign that lenders with subprime features pursue marketing practices and broker referral networks to reach groups of borrowers with comparatively good risk profiles. Since the demand-side models include a lengthy array of individual measures (along with underwriters' decisions on individual applicant risk factors) these patterns offer robust, multivariate evidence of spatial dimensions of subprime capital investment.

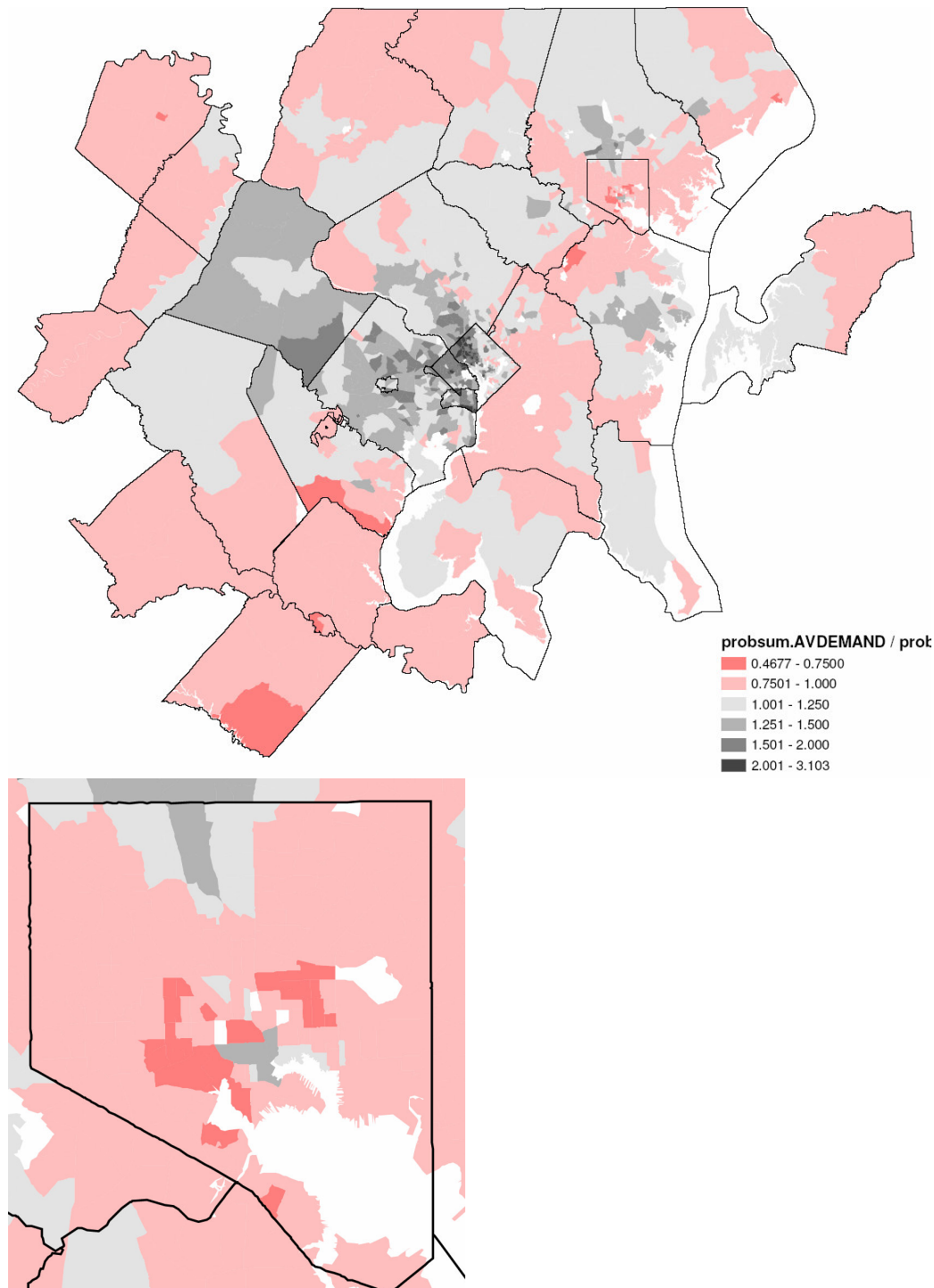


Figure 8. Demand-implied subprime segmentation probability, expressed as a ratio to supply-side probability estimate. *Source: calculations from Model 1 in Tables 4 and 5. Inset shows Baltimore City.*

Several of these patterns are, to be sure, unexpected and odd. Index values in Northeast and Southeast D.C. are thoroughly unremarkable, while extremely low values highlight the aging parts of outlying small cities (Martinsburg, West Virginia and Fredericksburg, Virginia), and neighborhoods on the edges of the region's large military bases: Quantico Marine Corps Reservation, Fort George G. Meade, and the Aberdeen Proving Grounds.²⁵ Yet the overall tapestry of demand and supply values is anything but random. It suggests a disproportionate flow of subprime capital into those parts of the region that have historically been neglected by prime, gold-plated mainstream lenders. Subprime profit opportunities are pursued by lenders, brokers, appraisers, investors, and other supply-side actors working to reach borrowers who have, or who believe that they have, few options in the prime, mainstream market (Apgar et al., 2004; Engel and McCoy, 2002). It is no surprise to see these effects most clearly in Prince George's County, the distant suburbs south of Washington, in West Virginia, and in Frederick County, Maryland (Figure 7). But the strongest evidence appears in the landscapes of Harvey's research a generation ago: the Baltimore inner city.

The Case of Baltimore

One of the spatial submarkets defined by Harvey (1974) included an irregular crescent of neighborhoods, about a mile and a half wide, encircling downtown and the elite enclave of Bolton Hill. In 1970 this "inner city" submarket was "dominated by cash and private loan transactions with scarcely a vestige of institutional or governmental involvement in the used housing market." (p. 261). The residuals from our model (Figure 7) fit almost perfectly within the inner-city submarket mapped by Harvey. Although we have not undertaken a full replication of Harvey's analysis of title transfer records, it is likely that most of the private cash or loan transactions and land-installment contracts he documented in 1970 have been replaced by the long menu of practices we know today as predatory lending. Between 1998 and 2002, institutions covered by HMDA loaned \$301 million backed by single-family homes, \$109 million of it by subprime lenders.

For individuals and communities, it is possible that today's subprime mortgage company is not all that different from a previous generation's small-time speculator-landlord pushing an installment-contract scheme. But in theoretical terms ~ and for purposes of scales of organizing, regulation, and policy ~ this is an important shift. In 1970, Harvey observed that "Class-monopoly rents are here realized by professional landlords who calculate their rate of return to match the opportunity cost of their capital." (p. 261). Today many more entrepreneurs are competing for access to class-monopoly rent, but for a time in the late 1990s the flood of capital into housing and land seemed to offer unlimited opportunities. On the front lines in the inner city, small-time brokers, realtors,

²⁵ For a particularly vivid example of the distinctive housing market circumstances identified by this modeling approach, consider the case of census tract 7401.02 in Maryland's Anne Arundel County. This tract posted an average demand probability estimate of 0.28 and a supply estimate of 0.38 on a total of 1,612 applications between 1998 and 2002. Subprime institutions accounted for 40 percent of all applications, and most mortgage activity (94 percent) was in the refinance and home improvement market. The tract is nestled on the north side of Fort Meade and on the eastern side of the multiple, varied institutions comprising the Maryland House of Corrections in Jessop. The 2000 Census enumerated slightly more than 2,400 inmates in the state prison complexes, in addition to 1,115 homeowner households (who account for 86 percent of the non-group quarters occupied housing units). Thirty percent of the tract's owner-occupied housing units are mobile homes, which helps to explain why Conseco Finance Servicing Corporation held the largest market share here between 1998 and 2002 (9.2 percent). Conseco acquired Green Tree Financial Corporation, the nation's largest mobile home lender, in 1998 just in time to confront full exposure to mounting credit problems among mobile-home borrowers and a wave of refinancings as interest rates fell; Conseco filed for Chapter 11 protection in late 2002, becoming (at the time) the third-largest filing in history behind WorldCom and Enron (Hamilton and Spinner, 2002). It is possible that the divergent model results for this tract are a product of the dominance of Conseco and similar institutions catering to mobile home owners, juxtaposed with lenders catering to higher-paid civilian employees working at Fort Meade, which houses 78 "partner organizations" from all four branches of the military, including the Defense Information School, the U.S. Army Intelligence and Security Command, the 694th Intelligence Group of the Air Force, and the National Security Agency (NSA). Approximately 10,000 military personnel work on base, along with almost 26,000 civilian employees (GlobalSecurity.org, 2004). Mortgage applications to the credit union serving NSA employees and subcontractors (Tower Federal Credit Union), however, come from neighborhoods throughout suburban Maryland, and are by no means clustered in this census tract.

appraisers, and home improvement contractors work in alternating relations of cooperation and competition to reap transaction fees whenever residents are convinced to enter into loan agreements. Then the loan originators earn points, fees, and other transaction profits on the initial loan, with opportunities for interest income and future refinance fees from the same borrower, or a loan resale that frees capital for other prospects. At least for those firms subject to disclosure rules, we can identify some aspects of their business. A ranked list of subprime lenders who dominate the competition in Baltimore’s inner city (Table 7) includes a number of obscure local or regional companies, but also several deep-pocket national firms with prominent (and not always positive) name brands: Ameriquest, Household, Conesco, and Citifinancial.

Table 7. Leading Subprime Lenders in Baltimore's Inner City.

Lender	Applications received	Market share			Location Quotient (B/C)
		of Baltimore	of inner	of regional	
		inner city A	city subprime B	subprime C	
Ameriquest Mortgage Company	741	4.1	7.0	8.1	0.86
Nationscredit Financial Services	594	3.3	5.6	2.4	2.35
Superior Bank	548	3.0	5.2	2.2	2.32
The Money Store	481	2.6	4.5	4.6	0.99
Advanta	373	2.0	3.5	2.2	1.59
Household Finance Corporation	327	1.8	3.1	5.9	0.52
Amresco Residential Mortgage Corporation	323	1.8	3.0	0.8	4.05
New Century Mortgage	314	1.7	3.0	1.4	2.11
Delta Funding Corporation	288	1.6	2.7	0.7	3.71
United Companies Lending Corporation	262	1.4	2.5	1.3	1.96
Conesco Finance Servicing Corporation	249	1.4	2.3	4.9	0.48
CIT Group/Consumer Finance, Inc.	234	1.3	2.2	1.2	1.79
Option One Mortgage Corporation	229	1.3	2.2	2.5	0.86
Wachovia Bank of Delaware	219	1.2	2.1	1.6	1.30
Mortgage Lenders Network USA	216	1.2	2.0	0.9	2.26
Citifinancial, Inc. of Maryland	201	1.1	1.9	1.3	1.50
Homegold, Inc.	175	1.0	1.6	3.4	0.48
Contimortgage Corporation	172	0.9	1.6	0.8	2.13
Key Bank USA	170	0.9	1.6	3.3	0.49
Green Point Mortgage Funding	169	0.9	1.6	2.8	0.58
American Business Financial	157	0.9	1.5	2.2	0.66
Homeowners Loan Corporation	155	0.8	1.5	1.6	0.90
Centex Home Equity Corporation	151	0.8	1.4	0.6	2.54
Banc One Financial Services	145	0.8	1.4	1.9	0.70
Beneficial Corporation	140	0.8	1.3	3.5	0.38
Resource One Consumer Discount	137	0.8	1.3	0.9	1.37
Equicredit Corporation of America	129	0.7	1.2	0.6	2.02
Citifinancial Mortgage	123	0.7	1.2	1.9	0.60
Equity One, Inc.	119	0.7	1.1	1.2	0.90
WMC Mortgage Corporation	111	0.6	1.0	0.8	1.32
Chase Manhattan Bank USA	110	0.6	1.0	3.5	0.30
IMC Mortgage Company	109	0.6	1.0	0.5	1.93
Chadwick Mortgage, Inc.	105	0.6	1.0	0.2	6.17
Ames Funding Corporation	103	0.6	1.0	1.1	0.87

These corporate entities allow us to trace the connections between Baltimore’s inner city and spatially-restructured networks of class-monopoly rent. Harvey’s (1974) “localized structures” for class-monopoly rent have been reconfigured as increased articulation of capital markets has allowed investors to gain access to profits that were once the exclusive domain of local speculators, brokers, and landlords. With the increasing macroeconomic capitalization of housing, however, local actors can continue to prosper, and in any event the development of new transaction methods creates new profits to compensate for long-run declines in interest-based yield spreads. The key point is that the local experience of class-monopoly rent is far more tightly integrated into national and international capital markets. To illustrate some of the salient aspects of these connections, we used the “follow the money” research methods recommended by Byers (2003) to trace the paths of investment and securitization

for four of the largest subprime lenders targeting Baltimore's inner city: Superior Bank, Amresco Residential Mortgage Corporation, New Century Mortgage, and Delta Funding Corporation.²⁶

Beyond their local activities in Baltimore, of course, each of these lenders has played a prominent role in regional and national markets ~ attracting ample press scrutiny and legal action. Superior, co-owned by one of the nation's wealthiest families (the Pritzkers of Hyatt Hotels), wound up tangled in lawsuits across the country alleging a wide variety of abusive and illegal practices; after severe losses on auto loans and high-risk mortgages, Federal regulators closed it in 2001 at a cost of \$500 million (Day, 2001).²⁷ Amresco specialized in loan servicing: describing the company's varied lines of business, a Moody's analyst remarked, "Servicers have run into difficulty from lending and investment, not from loan servicing." After a string of quarterly losses, Amresco was acquired in late 1999 by Lend Lease of Australia for its accomplished record in the "special servicer" market, where aggressive innovation is required to get people to keep paying; as the Moody's analyst put it, "These are the knuckle-breakers of the business." (Cohen, 2000). New Century has attracted comparatively little press attention, but got a bit of coverage after making a loan of \$387,000 to a 60-year old man whose primary income was \$1,000 per month from Social Security disability benefits; the adjustable-rate note began at 9.5 percent, nearly 4 percent above the prime-credit rate prevailing at the time (Spencer, 2003). And Delta Funding Corporation is the largest subprime lender in the state of New York. Delta was forced to pay \$12 million in fines and restitution as part of a 1999 settlement with the State Attorney General. The next year a trio of federal agencies (the Department of Justice, the Department of Housing and Urban Development, and the Federal Trade Commission) accused Delta of paying kickbacks and unearned fees to brokers, and of charging African American females significantly higher rates than otherwise identically qualified white males (Mayer, 2000). For several years Delta had managed to make loans with illegal penalty interest rates as high as 24 percent (at a time when conventional rates were edging towards 7 percent), and New York Attorney General Eliot Spitzer charged that the lender explicitly used low loan-to-value ratios to provoke defaults and ensure that foreclosure auctions would yield ample profits (Santiago, 2000). Delta is particularly noteworthy for our purposes, because the 1999 Attorney General's investigation was inherently geographical ~ documenting the close correspondence of the lender's loan patterns with census tracts at least 80 percent African American in East New York, Bedford-Stuyvesant, and Jamaica, Queens (Kennedy, 1999).

Securitization and Capital Conduits

Each of these lenders were regular players in securitization deals, and thus they provide a window on the anatomy of contemporary structures of class-monopoly rent in local mortgage markets. To illustrate some of the salient connections, we analyzed what investors were told in the prospectus supplements accompanying the most recent mortgage-backed security offerings filed at the Securities and Exchange Commission (Superior Bank, FSB, 2000;

²⁶ We chose these lenders for two key reasons: 1) they are the largest subprime actors with disproportionate representation in the Baltimore inner city neighborhoods defined in our multivariate analysis, and 2) they were directly involved in securitization deals that can be traced with public records. Nationscredit, for instance, meets the first criterion but not the second, since it was not directly involved in any mortgage-backed securities offerings between 1998 and 2002. It is likely that Nationscredit simply pursued private sales to institutional or individual investors before any of the original loans were packaged into asset-backed securities to be sold on Wall Street. Our four case study lenders, by contrast, went directly to underwriters who prepared securities offerings, and thus their loan pools are described in public disclosures to the Securities and Exchange Commission (SEC). Estimates of supply model 2 (Table 7) predicting the distinguishing characteristics of these four lenders as a whole yield a robust model fit, with a Nagelkerke index of 0.52, and 97.1 percent of all observations correctly classified. Model results indicate that these lenders focus heavily on refinancing and home improvement lending to African Americans (and have higher rates of racial non-reporting), while completely avoiding the regulations and scrutiny that come with FHA lending or sales to the GSEs. Controlling for all other factors, these lenders are much less locally-oriented, and judging by the demand instrument, their applicant pool is only slightly inferior (a one-standard deviation increase in the demand instrument yields an odds ratio of 1.16). Together, these four lenders received 61 thousand applications across the entire study area, mostly in 1998, 1999, and 2000.

²⁷ Paul Sarbanes (D-MD), Chair of the Senate Banking Committee, scheduled hearings to question the FDIC and other regulators over Superior's collapse. The hearings were scheduled for September 11, 2001, and we have been unable to find any evidence that the hearings ever occurred.

Amresco Residential Securities Corporation, 1999; New Century Mortgage Securities, Inc., 2003; Delta Funding Corporation, 2001). These materials are not exactly ideal as research tools, but there are remarkably candid and valuable snapshots of investor behavior and institutional context buried in the several hundred pages of each supplement.²⁸ The most recent offerings for these lenders include securities pools of \$546 million of Superior loans (June, 2000), \$209 million of Amresco notes (October, 1999), \$1.14 billion for New Century (December, 2003), and \$180 million of Delta mortgages (October, 2001).

The investor supplements describe an enterprise of extraordinary complexity designed to support investors' pursuit of the simple goal of maximum risk-adjusted yield. The prospecti offer a counterpart to the usual biases in the literatures on aggregate lending trends or surveys of borrower behavior. Here we see the concerns and motivations of the wealthy individual or institutional investor. Three main themes emerge. First, high-risk subprime capital finds its way through securitization to some of the most familiar investment-bank trademarks that appear regularly in the business press as well as the global-cities and international banking literatures. Underwriters for the case studies securities (i.e., the investment banks who take the deals public and sell to individual dealers and then to investors) include Merrill Lynch, Prudential Securities, Lehman Brothers, and in the case of New Century's billion-dollar trust, a partnership between Bank of America, Citigroup Global Markets, Morgan Stanley, and UBS. Second, the deals mirror the cross-collateralization and diversification techniques (of the sort documented by Eggert, 2003, 2004, Engel and McCoy, 2003, 2004, and others) that extract respectable yields even from high-risk loans. These techniques have severed the traditional mutual interest of all parties in avoiding individual cases of default (Eggert, 2003). Each of the deals analyzed involves a mixture of subordination, tranche structure, and overcollateralization that offers multiple certificate classes, each tailored to investor risk-adjusted yield preferences. By design, the loan pools include heterogeneous risk and return profiles: each blends fixed- and adjustable-rate loans, and loans for various purposes, with a dizzying array of detailed underwriting and pricing specifications. Obviously, our concern here is high-cost credit. One quarter of the adjustable-rate package of Superior loans carried initial interest rates over 12 percent, and almost as many of its fixed-rate notes were balloon-payment loans. More than two-thirds of the \$824 million in conforming notes offered by New Century were subject to prepayment penalties lasting at least two years. More than four-fifths of Delta's offering was covered by some duration of prepayment penalty, helping to protect the pools' weighted average interest rate of 10.53 percent. When the pool is creatively structured by repayment tranche, even quite high-risk borrowers can be included in order to boost yields. Collateral cushions on the underlying loans, and on the notes through overcollateralization, are also used to protect investors. Amresco's filing is particularly revealing on the borrower risks that can be included with these methods. Amresco "focuses on originating nonconforming mortgage loans to borrowers who have substantial equity in their residences," (p. 36), and almost all of the individual loans in its offering were risky enough to have been spurned by other purchasers.²⁹ Most of Amresco's pool involved cash-out refinance loans, but much of the weighted average interest rate (9.79 percent) was shielded by lengthy prepayment penalty clauses (see Table 8).³⁰ This is a fairly high-risk package: notes designated as 'B' or

²⁸ It is impossible to follow sales of individual loans on the secondary market, or to identify groups of loans at any geographic resolution below the state level. Instead, the analyst can only draw inferences about inter-scalar relations by 1) identifying specific lenders that stand out in a particular place (as in our modeling approach) and 2) analyzing the national operations of these lenders that is presented to investors as part of securities sales (Byers, 2003). Another limitation is temporal: originators often hold loans for varied periods of "seasoning" before packaging them for sale. Loan pools are usually designed to have wide variation in origination dates (and in other features) to maximize diversification and safety.

²⁹ In required disclosures of risk, Amresco noted the adverse selection of the loan pool, stating that 92 percent of the loans "have been previously offered for sale to purchasers and were excluded from purchase, or purchased and subsequently repurchased by the originator for a variety of reasons." About one-third were rejected or repurchased because "of what purchasers believed to be potential disclosure or documentation deficiencies under federal or state law." (Amresco Residential Securities Corporation, 1999, suppl. p. 7).

³⁰ Prepayment penalties are a standard mechanism for protecting the lender (or investor) from the deleterious effects of receiving a loan payoff prior to maturity. Prepayments are more likely when interest rates fall, creating the risk that the lender (investor) will not be able to reinvest the principal at the same rate of return. In the competitive prime market, accepting a prepayment penalty usually allows a borrower to get a reduced interest rate. There is limited evidence of similar tradeoffs in the subprime market.

below, for instance, permit several thirty- or sixty-day delinquencies, as well as a discharged bankruptcy within the previous 18 months (so long as there was no delinquency on re-established credit) (Table 8). Nevertheless, securitization is explicitly designed to stratify, balance, and price the risks such that even loans to very risky borrowers can be included in successful deals. MBS issues are generally quite successful. Superior's 2000-2 issue maintained its investment ratings until days before the bank's collapse.

Table 8. Selected Characteristics of the Amresco Pool.

Purpose	Number of Loans	Principal balance (\$ thousands)
Cash Out Refinance	1,231	102,463
Purchase	720	55,337
Rate/Term Refinance	557	50,906
Home Improvement	3	141
Construction Permanent	2	117
<i>Total</i>	2,513	208,964
Prepayment Penalty Term (years)	Number of Loans	Principal balance (\$ thousands)
0	760	49,216
0.01-1.00	13	1,259
1.01-2.00	870	91,659
2.01-3.00	64	4,963
3.01-4.00	3	172
4.01-5.00	803	61,695
<i>Total</i>	2,513	208,964
Credit Level	Number of Loans	Principal balance (\$ thousands)
A	577	57,542
A-	507	49,531
B	628	52,874
C	618	39,127
D	183	9,889
<i>Total</i>	2,513	208,964

Source: Amresco Residential Securities Corp. (1999).

Third, securities disclosure regulations provide investors with intimate (albeit selective) details of corporate organization, loan underwriting practices and staff compensation policies, broker relationships, insurance provisions and international transaction clearinghouse procedures, and legal and legislative developments. The prospectus supplements offer a full-blast firehose of cogent analysis and rich empirical description; but the seasoned dealer or investor no doubt sifts through all this detail precisely as Harvey would ~ carefully evaluating all moments in the circulation of capital, from the expropriation of surplus value from the homeowner to its allocation amongst various (and competing) owners of capital. Anything that enhances this flow, or that threatens it, is examined with extreme care. A striking illustration is Delta's filing, which documents each of the lawsuits filed against the originator, and then proceeds to offer assurances that Delta "believes that it has meritorious defenses and intends to defend this suit, but cannot estimate with any certainty its ultimate legal or financial liability, if any, with respect to the alleged claims." (Delta Funding Corporation, 2001, p. S-16; see also pp. S-17 to S-19). Securitization offers investors some level of protection from these threats (Eggert, 2003), but the rising tide of anti-predatory community activism and legislation in the last few years has aroused new concerns. Therefore, prospectus supplements now often include longer sections on legal considerations. In addition to longstanding disclosures (i.e., whether any of the loans are "high-cost" as defined by the Home Ownership and Equity Protection Act of 1994), there are updated discussions of federal and state legislative proposals. New Century's billion-dollar offering notes that "a number of legislative proposals have been introduced at both the

federal and state level that are designed to discourage predatory lending practices” by regulating certain loan terms or enhancing disclosure rules (New Century Mortgage Securities, Inc., 2003, p. S-13). Here we see the investor concern that has been responsible for aggressive lobbying and the decisions of bond-rating agencies (Moody’s, Standard and Poor’s, Fitch) to thwart the most important legislative response to predatory lending: the provision for assignee liability that would take the profit out of abusive practices: “The originator’s failure to comply with these laws could subject the trust, and other assignees of the mortgage loans, to monetary penalties and could result in the borrowers rescinding such mortgage loans against either the trust or subsequent holders of the mortgage loans” (New Century Mortgage Securities, Inc., 2003, p. S-13).

Conclusions

“...the homeownership resulting from federally backed home finance policy is largely an illusion. Most owners have mortgages on their homes. If the mortgaged homeowner doesn’t pay the mortgage, he’s out. And if the renter doesn’t pay the rent, she’s out. When the crunch comes, owning and renting are not so different.”

Don Krueckeberg (1999, p. 23).

“...we find ourselves without a sophisticated language of class precisely at the time when, globally, class is being reasserted with a vengeance.”

Neil Smith (2000, p. 10111).

Homeownership is one of the few enduring bipartisan pillars of the American political economy. Implicit and direct subsidies to middle-class and wealthy homeowners have endured for half a century, but in the last decade homeownership policy has been redirected to lower-income households, racial and ethnic minorities, recent immigrants, Native Americans on reservation lands, and others constructed as “new” or “underserved” markets. This policy emphasis includes selective elements of a progressive agenda to fight discrimination and poverty, but it is also woven tightly into the ongoing effort to privatize, devolve, and dismantle the remnants of the redistributive welfare state. Welfare as we knew it has come to an end. But homeownership remains a popular and bipartisan solution to an expanding menu of social, economic, and policy dilemmas.³¹ Unfortunately, the capitalization of homeownership policy has simply reproduced old inequalities through new institutional relations that retain the necessary illusion of individual ownership, freedom, and choice.

This is not to dismiss the struggles of those who fought individual and collective battles against discrimination, redlining, and exclusion (Squires, 1992, 2003). But we do suggest that inclusion has been a bittersweet success, and that understanding its limits requires a careful reckoning with the fundamental inequalities of class-monopoly rent. The expansion of debt-financed ownership has exacerbated the tensions of exclusionary rights, which are only valuable if some people are denied access to them. A rising ownership rate for low-income households necessarily requires a dilution of the material benefits for new owners, or a greater extraction of resources from working-class renters; evidence on the uncertainty of home price appreciation for low-income owners (Retsinas and Belsky, 2002), and the worsening rental crisis in many American cities (Stegman et al., 2000), suggests that both of these trends have worsened housing inequalities. At the same time, an increasing proportion of lower-income homeowners are woven into complex, multi-faceted, and multiply-scaled relations of class-monopoly rent. Our analysis should not, however, be taken to imply that there is anything inevitable about the contemporary structure and geography of class-monopoly rent. Predatory lending has become a key battleground between industry advocates, legislators from the local to the federal levels, community activists, and attorneys and legal scholars. It is questionable whether the “movement” represented by the alliances, tensions, and tactics of those

³¹ It is notable that the Bush Administration’s housing policy has made few changes to the homeownership promotion strategies of the Clinton years, while Section 8 certificates and other rental subsidies are slated for substantial reduction.

fighting predatory lending could measure up to the social-movements benchmarks of, say the 1960s Civil Rights movement. But the movement has achieved important tactical victories, almost always in association with an explicit challenge to economic exploitation. The distinctive history and context of American homeownership has certainly muted direct references to class, but this “crucial political dimension of social difference” (Smith, 2000, p. 1011) is at the heart of the community reinvestment movement.

In a previous generation, renters understood that the rent collector did not simply represent a scarce factor of production (Harvey, 1974), and the landlord was clearly understood in the context of his class position. Today’s landlords are gradually coming into view. Organizers, attorneys, and researchers are working to “follow the money” behind local predatory schemes (Byers, 2003). The National Community Reinvestment Coalition continues to publicize its annual lists of “best” and “worst” lenders, while the Woodstock Institute monitors institutions engaged in “slash-and-burn” financing. There are calls “to hold banks accountable, from the Bronx to Buenos Aires, Beijing, and Basel” (Lee, 2003). And there are more and more efforts to draw direct connections between unscrupulous local predators and the Armani-clad bankers and securities dealers extracting their share of the class-monopoly rents that continue to structure the American city. Capital is the landlord, but the renters are getting organized.

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