

A SPECIAL REPORT

**INSIGHTS INTO
THE MINORITY
HOMEBUYING
EXPERIENCE**

**The Mortgage
Application
Process**



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This special report funded by the
Research Institute for Housing America

A study conducted by **ReedHaldyMcIntosh**



Under a cooperative agreement with the U.S. Department of Housing and Urban Development, the Mortgage Bankers Association of America commissioned the firm of ReedHaldyMcIntosh to conduct focus groups to improve our understanding of the mortgage application process in the African-American and Hispanic/Latino communities. *Insights into the Minority Homebuying Experience: The Mortgage Application Process* summarizes ReedHaldyMcIntosh's findings. The results will be incorporated into a broad-based telephone survey that will explore differences in how minority and non-minority families look for mortgage credit.

Four sessions were held in Chicago, Illinois, in early 2003. High- and middle-income households that recently applied for a home mortgage were brought together to discuss their experiences. Participants from both communities identified the lack of experience and knowledge about mortgage loans, credit and the mortgage application process as the major barrier to obtaining home mortgages. Not surprisingly, a recurrent theme in their search process was the desire to find hands-on help to bridge the gap.

In general, participants in the higher income groups were more successful in overcoming the barriers and were more comfortable with the process. However, almost all felt that real estate agents, lenders and their local governments were, or could be, important in improving the process mainly by providing resources to assist the prospective homeowner.

Issue 1

Difficulties with Credit, Credit History and Financial Management

A substantial minority of homebuyers from the African-American and Hispanic/Latino communities reported having credit blemishes or poor credit. Successful mortgage applicants often reported that they took classes or worked with a knowledgeable person to improve their financial management skills and to understand how their credit would be evaluated. Many took steps prior to applying for a mortgage to address outstanding credit issues and, thus, improve their credit scores. Group participants emphasized the importance of:

Understanding credit scoring

- Most of the successful mortgage applicants learned about, or were advised on, how mortgage lenders and rating agencies evaluated and scored applicants prior to applying for their mortgages.
- Those who learned about, or were advised on, credit matters were much more confident that they were treated fairly in the mortgage application process.

Repairing one's credit history

- Many successful applicants worked to determine their credit scores, and, if necessary, repaired their credit standing as the first step in the homebuying process.
- Those who had worked to improve their credit scores felt that this activity paid off in better mortgage rates and terms.

I worked with my sister-in-law, a bank officer, to build up my credit score a year ahead.

–Respondent in the upper-income Hispanic/Latino focus group

Issue 2

Lack of Experience and Prior Understanding of the Mortgage Application Process

[People] should take a workshop. Hispanics especially; 90 percent don't know what they are doing.

—Respondent in the moderate/low-income Hispanic/Latino focus group

Although knowledge levels varied widely, many African-American and Hispanic/Latino mortgage applicants had a limited understanding going into the mortgage application process. Both those who felt they were well-prepared and those who felt they were not well-prepared emphasized the importance of:

Understanding the terminology of the homebuying process

- Participants thought it was important to understand the types of documents needed for a mortgage application.
- In retrospect, buyers felt it would have been helpful to understand the roles and responsibilities of the various players in the mortgage application and approval process.

Understanding the sequence of steps to follow in the mortgage application process

- Most first-time homebuyers in the groups learned about this through trial and error.

Knowing how to obtain unbiased advice

- Most minority mortgage applicants were unsure about where they can turn for unbiased advice directly relevant to their situation.
- Many African-American and Hispanic/Latino participants were unaware of available educational programs and counselors.

Defining their own financial capabilities, knowing application requirements beforehand and understanding the many mortgage options available to them

Issue 3

Prequalification and Realistic Assessment of Financial Qualifications

Several participants found prequalification to be a useful tool, but others did not understand how it could help them. In other situations, the informal preapproval amounts for mortgages and monthly payments were unrealistically high, even from the perspective of the eager potential homeowner. Many focus group participants suggested that they do not understand:

The role of prequalification in the application process

How and why to get prequalified

- Who can legitimately provide prequalification for a potential homebuyer?
- What goes into prequalification?
- How does prequalification help the potential homebuyer? What exactly does it guarantee?

How to determine if the prequalification amount and associated mortgage payment would be realistic or appropriate to the financial burdens that the mortgage applicant wished to assume

- A number of focus group participants reported that when an interested party did the prequalification, the approved loan amount and terms represented more of a financial burden than they felt was suitable for their families.
- Several participants emphasized the importance of a prequalified calculation that includes all ancillary costs of homeownership and other personal financial obligations.

We got preapproved to see what we could afford. My wife's best friend, a real estate broker, set it up for us.

—Respondent in the moderate/low-income African-American focus group

Issue 4

Finding Trusted Friends/Advisers with Knowledge of the Business

In my family, I am the first to buy a house. My brothers will benefit from my experience and knowledge.

—Respondent in the low/moderate-income Hispanic/Latino group

The greatest differentiator between those from the African American and Hispanic/Latino communities who were happy with their home purchasing experience and those who were not was the presence (happy) or absence (not happy) of trusted advisors. The experience of participants in the focus groups showed that potential homebuyers need to understand:

That the homebuying and mortgage application processes are complicated financial transactions requiring knowledge and skill to complete successfully

For most families credit clean-up and financial management skills benefit greatly from the assistance of knowledgeable and trustworthy friends and advisers

The average person also needs trustworthy and expert assistance in watching out for their interests throughout the homebuying and mortgage application processes

Not everyone can easily find a trusted and knowledgeable adviser

- The lack of friends and relations with the necessary expertise was reported more frequently among participants with lower income, less education and low fluency in English and among those who were new to the area.

The mortgage applicant needs to follow the adage “buyer beware”

- Some participants felt that the actions of real estate agents and mortgage loan officers were not in their interest.
- Among those less familiar with the process, choosing a “bad” adviser turned out to be a problem.

Issue 5

Finding a Mortgage and Evaluating Mortgage Offers

I have been a landlord's son all my life, but it was very tricky and time-consuming when it came to finding the best deal.

—Respondent in the moderate/low-income African-American focus group

Participants used several avenues to find mortgages. The more knowledgeable they were about the process, the more likely they were to feel that their mortgage process was successful. Those who were most savvy were knowledgeable about:

The basics of the mortgage finance system

- Most African-American and Hispanic/Latino participants felt, in retrospect, that it was important to understand the basics of mortgage origination, lending and servicing.
- Participants used a wide variety of sources to get their loans. They felt the process was more confusing if they did not understand the advantages and disadvantages of independent mortgage firms, banks, credit unions and special governmental programs.
- Some reported that they were given a range of mortgage options. A majority was not provided with, or did not seek, a variety of mortgage options.

The potential advantages and disadvantages of real estate agent referrals to sources of mortgage credit

- Participants without personal contacts were more likely to rely on real estate agent referrals with uneven results.
- Those who were the most dissatisfied with the mortgage application process were usually those who were referred by someone involved in the real estate transaction.

How to determine if the mortgage offer is fair

- Most homebuyers did not actually comparison-shop for the best terms for their mortgage. Many did not think such comparisons were possible.
- Most thought that the terms for their mortgage were reasonably fair. They determined this by using very general comparisons such as information from friends, from the Internet or from experts in the field.
- A substantial number of participants were just happy to get a “yes” to their mortgage application, so they did not ever consider the possibility of getting better terms for their mortgage.
- The few participants who considered multiple mortgage applications to permit closer comparisons were discouraged from doing this by the penalties associated with repeated requests for credit scores.
- Those who thought that something was not fair about their mortgages had a hard time identifying particular elements that were not fair, since they tended to be those with the least expertise and general knowledge about the process.

Focus Group Highlights

Highlights from focus groups among African-Americans and Hispanics/Latinos who had applied for a mortgage within the past year.

Highlight 1

The mortgage application process seems to work reasonably well for most group participants.

Highlight 2

Networks of trusted individuals who are knowledgeable about the mortgage application process were viewed as critical for almost all of these mortgage applicants. Most mortgage applicants do not consider themselves experts and generally feel that they must rely on those more knowledgeable than themselves for advice in what is a complicated and often stressful transaction.

Highlight 3

Participants understand the need of lenders to ensure the safety of their loans. They do not always understand how particular pieces of information requested of them are related to that goal. In particular, quite a few of the participants considered the application process to be somewhat invasive of their privacy, particularly since they did not understand how various pieces of information are related to determining their qualifications as borrowers.

Highlight 4

Although most participants were not able to cite specific personal situations in which they felt that they were discriminated against in the mortgage application/approval process, most felt, with varying degrees of vigor, that homebuyers from the African-American community were discriminated against in the homebuying process. They focused their attention more, however, on real estate agents and felt that they received unequal treatment, especially in the selection of housing available to them.

Highlight 5

Among the four groups, only the lower/moderate-income Hispanic/Latino group expressed concern about possible predatory lending practices associated with home mortgages. Participants in this group had the fewest connections with trusted sources of information and guidance about the homebuying process. They also were the most likely to lack the education and knowledge to negotiate the mortgage application and homebuying process on their own. They tended to be the most reliant upon and least trustful of real estate agents. They were more likely than participants in other groups to rely on real estate agents to connect them with mortgage lenders, while at the same time generally feeling least secure that these recommended lenders were working in their interest. Finally, participants in this group were more likely to express concern about being victimized by members of their own Hispanic/Latino community after they turned to them and trusted them. Higher-income participants from the Hispanic/Latino community did not express these same concerns. They had lived in the area longer, were better educated, had better command of English and, most important, had developed better advice networks among friends and acquaintances.

Focus Group Methodology

These findings are drawn from focus groups that were held in Chicago, Illinois, in January 2003. Two groups with African American participants were held; one with a household income of \$50,000 or more and one with a household income below \$50,000. Two additional groups were held with Hispanic/Latino participants broken into the same income categories.

All focus group participants had applied for mortgages for their personal residences within the past year or were in the process of mortgage financing at the time of the groups. The majority of participants were engaged in or had just completed their first home financing experience. Others had recently refinanced their mortgages. A few participants from the groups had previous experience in obtaining financing for homes before their most recent home mortgage financing experience.

The sessions were led by expert moderators with extensive experience in market research in the African American and Hispanic communities respectively.



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