

Financial Constraints and the Racial Housing Gap (Arpit Gupta, Christopher Hansman, Pierre Mabile)

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Summary and Contribution

- ▶ How much do financial downpayment constraints contribute to racial housing wealth gap and spatial misallocation?
 - ▶ Main friction: higher opportunity areas impose stricter limits on leverage
 - ▶ Bunching, and differences-in-differences design
 - ▶ Equilibrium spatial life-cycle model that allows to run counterfactuals
- ▶ Findings
 - ▶ Large role for financial constraints in perpetuating racial (housing) wealth disparities
 - ▶ Downpayment constraints bind systematically more for Black households than white households
 - ▶ Constraints perpetuate spatial mismatch by race and thereby lead to history dependence
- ▶ Policy implications: A combination of relaxed financial downpayment constraints and increased housing supply can reduced the housing gap between Black and white households as well as improve spatial misallocation

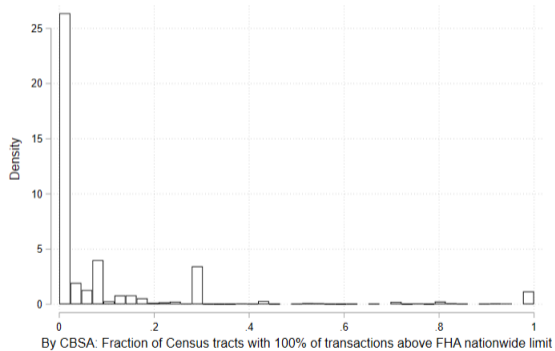
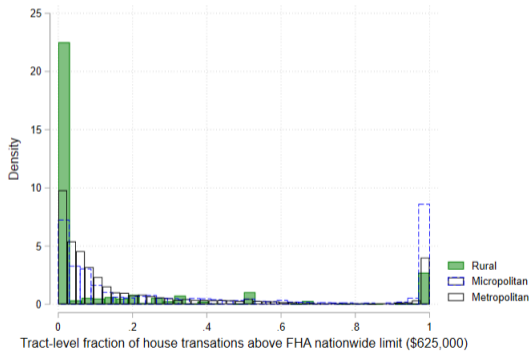
Highlights of the paper

1. Research question with crucial implications for policy making and reducing racial inequality → Addressing spatial misallocation (Hsieh & Moretti, 2019) that leads to inequality and reduced productivity of cities
2. Elegant model that includes only the key elements to give a 2×2 cross-sectional distribution of individual type and location choice
3. Directly use reduced form variation to calibrate the model → Key reduced-form moment: responsiveness of Black households' borrowing to availability of FHA mortgages
4. In the counterfactual, linking of downpayment constraints to housing supply policies and examining the interaction

Comment 1: Model interpretation – Locations and amenities

- ▶ Motivation for the paper comes from neighborhoods with high and low opportunities, such as better job opportunities, but also higher quality public schools, and intergenerational mobility
- ▶ To remain tractable, the model distinguishes between high- and low opportunity locations → Spatial models often tend to feature an amenity distribution
- ▶ More detail on what a high-opportunity versus a low-opportunity location in the model translates to in the data
 - ▶ Seems it's tied to the availability of FHA loans → How many areas feature no FHA loans?
 - ▶ Should we think of high-opportunity areas as entire cities/ commuting zones or neighborhoods?
 - ▶ Income differences arise from skill sorting and different opportunities → Opportunities might be endogenous to the people living in the locations themselves
 - ▶ Does the income process capture location-specific amenities such as good public schools in a flexible way? → What is the implicit assumption on sorting on amenities?

Relatively few Census Tracts are entirely ineligible for FHA loans



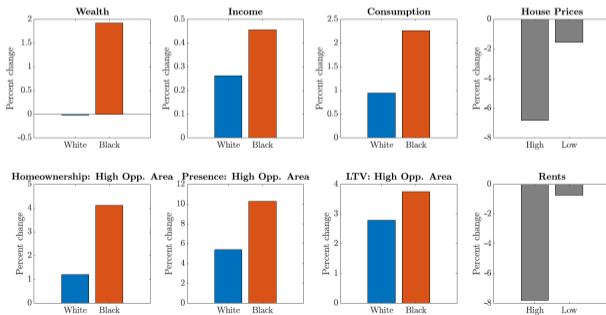
Equilibrium: Relax leverage limit in high-opportunity locations

- ▶ Counterfactuals raise interesting questions about the choice between renting and owning: Rents fall both in the high and the low opportunity neighborhood
- ▶ My prior was that rents would not fall, but certainly that rents would fall more in low-opportunity neighborhoods than high-opportunity neighborhoods
- ▶ What is driving these results?
- ▶ Seems to suggest that households are not wanting to be renters in high-opportunity neighborhoods? Which calls in question how amenities are being captured here apart from the wealth accumulation channel
- ▶ Would be interesting to also examine chosen squarefootage → Are new renters in high-opportunity areas predominantly consuming very little housing?
- ▶ Is there a cutoff value for relaxing LTV when rents fall rather than rise in the high-opportunity neighborhood or do they always fall? → Important policy consequences

Equilibrium: Housing supply

- ▶ Is new supply rented or owned?
- ▶ Is the overall population fixed in the counterfactual simulations? → How much of price decreases is mechanical?
- ▶ As before, would be helpful to see the consumed quantities of housing

FIGURE 8: HIGH HOUSING SUPPLY IN HIGH-OPPORTUNITY AREA



Comment 2: Use the reduced form exercise to discuss variation across neighborhoods

- ▶ Clarify exactly how treatment is defined → How many tracts are there where all loans are above the FHA national limit?
- ▶ Reduced form allows you to estimate a key parameter that you can then match with the model – the elasticity of Black borrowers with respect to the share of FHA loans
- ▶ Additionally, use it to fill in gaps from the model → Show us a mapping from these areas to the two geographies in the model
 - ▶ Which places are treated, i.e. in the model these will be on the verge between high and low-opportunity areas
 - ▶ Rural/ urban / suburban status / spatial distribution / amenities
 - ▶ Within or across cities: How do we think about commuting? I.e. can you access (labor market) opportunities by living nearby in a cheaper area

Validate the model more: Show us more moments that are key in the model

- ▶ Look at the share of renters of different races as an outcome (right now this is mostly suggestive)
- ▶ Is the difference in racial composition driven by the lack of new in-movers or an increase in out-movers?
- ▶ Show us housing supply constraints/elasticities in treated areas compared to control areas (WRLURI)
- ▶ Change in house prices in treated areas (the model predicts that demand will fall)
- ▶ Lifecycle profile (Figure 6) seems like something you can directly compare in the data as well, this would be nice as another validation exercise

Comment 3: Identification of key parameters

- ▶ Model fits many targeted moments well but seems to be underestimating the fraction of Black households choosing high-opportunity neighborhoods (and therefore also fraction of Black home owners)
- ▶ Among non-targeted moments, Black-white gaps are larger in the data than predicted by the model
- ▶ Suggests
 - ▶ Something missing from income process
 - ▶ Black households more price sensitive in reality

TABLE 3: MODEL FIT: TARGETED MOMENTS

Variable	Data	Model
Avg house price high-opportunity	455,000	455,000
Avg house price low-opportunity	225,000	225,000
Avg rent high-opportunity	1,588	1,588
Avg rent low-opportunity	1,008	1,008
Avg income high/low-opportunity	1.70	1.76
Avg income white/Black	1.73	1.70
Share white living in high-opportunity	0.19	0.21
Share Black living in high-opportunity	0.08	0.15
Avg moving rate to high-opportunity white	0.02	0.03
Avg moving rate to high-opportunity Black	0.02	0.02
Homeownership white in high-opportunity	0.68	0.72
Homeownership Black in high-opportunity	0.48	0.55
Homeownership white in low-opportunity	0.67	0.69
Homeownership Black in low-opportunity	0.45	0.46
Avg wealth/avg income	4.50	4.28
Avg house price/avg income	4.05	4.03
Avg rent/avg income	0.20	0.18
Avg default rate	0.02	0.02
Quasi-exp. treatment effect: $\frac{\Delta(\pi_{sh}^{high})}{\Delta(\rho_{sh}^{high})}$	0.098	0.101

Bindingness of the LTV limit

- ▶ Bindingness of LTV limit plays a key role for the identification of CES parameter ϵ
- ▶ Higher bunching indicates households have a high valuation for the neighborhood as compared to having higher consumption
- ▶ The decision to rent versus own tells us about this, choosing to rent a small space also implies having a high valuation for the neighborhood
- ▶ Can you directly target the fraction bunching at the limit or add this moment to the untargeted moments

Comment 4: Another suggested counterfactual

- ▶ Much of the debate around reducing racial inequality around neighborhoods now centers around improving given neighborhoods rather than incentivizing households to move away
 - ▶ Chetty et al (2020)
 - ▶ Kelly & Ellen (2022)
- ▶ Can you do a counterfactual that simulates these kind of policies? I.e. increases opportunity in currently low-opportunity neighborhoods?
- ▶ One way to think about it in this model is to change the income process by increasing μ_j with and without additionally relaxing the loan limit or housing supply
- ▶ Or introducing a third type of area?

Conclusion

- ▶ Highly important policy question: How do financial constraints – especially in housing markets – impact the gap in housing wealth between Black and white households and spatial misallocation
- ▶ Model and reduced form that fit together and give predictions about ownership status, consumption, savings, and access to high-opportunity areas across races
- ▶ If governments relaxed leverage caps and additionally increased supply of housing, Black households would be able to move to higher-opportunity areas at lower costs and accumulate more housing wealth, thereby beginning to close the housing gap
- ▶ Reduced form analysis can be used to further supplement some elements of the model
 - ▶ What is behind high-opportunity housing locations?
- ▶ Equilibrium price effects are still a bit puzzling, suggesting that some aspects of location sorting are not fully captured