An often heard criticism of regulation is that it reduces the availability of mortgage credit. High prices and onerous terms are excused as necessary to match the high risk of lending to certain borrowers. Critics argue that restrictions on price or terms will prevent the market from extending credit to the riskiest borrowers.

But the claim that risk accounts for rate was clearly not true in many mortgage loans during the run-up to the 2007 crisis. As explained further below:

? Many loans were written with no consideration of risk;\(^\text{280}\)
? Many lower-risk borrowers were placed in higher-priced loans;\(^\text{281}\)
? Even when creditors tried to underwrite for risk, it is unclear they are able to do so successfully;\(^\text{283}\)
? Race seemed to be as much a factor in determining price as risk;\(^\text{283}\)
? The high-risk label allowed lenders to generate higher income, leading lenders to steer creditworthy borrowers to high-rate, high-risk credit\(^\text{284}\)—then the high rate and predatory nature of the loan creates the risk.\(^\text{285}\)

Footnotes

280 [280] See § 1.3.4.2 [1], infra.

281 [281] See, e.g., Sumit Agarwal, John C. Driscoll, Xavier Gabaix, & David Laibson, The Age of Reason: Financial Decisions Over the Lifecycle [2] 8–9 (Feb. 11, 2008), available at http://ssrn.com (older and younger borrowers pay more for credit than midlife borrowers in home equity loans primarily because they underestimate the value of their homes and apply for loans with a higher loan-to-value ratio than needed; lenders conduct their own appraisal of the value of the property and re-price the loans higher if the consumer overestimated the value, but do not re-price the loans lower when the consumer underestimates the value of the home); id. at 30–31 (older borrowers generally more credit worthy than midlife borrowers, but older borrowers pay more for credit across several markets).

282 [282] See § 1.3.4.3 [3], infra.

283 [283] See § 1.3.4.4 [4], infra.


285 [285] See § 1.3.4.5 [5], infra.

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