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Redlining Is Only One of the Factors Affecting the Health of an Area

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Redlining — the reluctance of banks to make mortgage loans on buildings in declining areas — has recently attracted much simplistic outcry from politicians, an appropriate number of scare newspaper headlines and some prodding legislation; but there has been little serious discussion either of the real causes of the problem or of alternative solutions and their probable long-term effects.

The heart of the problem — the conflict between the best interests of the prudent lender and the financial desires of the would-be borrower — invariably is ignored as spokesmen for the respective sides focus on symptoms rather than on causes and on palliatives rather than on cures.

A rising chorus is being heard demanding access to mortgage credit regardless of the risk factors or experience involved, at or below rates charged for conventional loans, and increasingly the claim is made that noneconomic investment in declining areas is the proper obligation of the conventional banking system.

Two key facts — that the first duty of a savings institution should be to protect the savings entrusted to it and that literally billions of dollars of capital value of central-city real estate have evaporated in a handful of years due to vanishing jobs and declining populations — seem to have been forgotten.

The complex of economic factors affecting the life and death of cities, the nature of the political climate and its economic impact, and finally the legitimate rights and obligations of all parties involved, do not seem to enter the thinking of the most voluble players in this deadly serious, potentially destructive game.

It is true of course that availability of mortgage credit is one of a number of significant factors affecting the health of a neighborhood, but it is, after all, only one of them. And the extent to which a change in credit availability is a result rather than a cause of decay is almost impossible to determine.

When the Census Bureau recently reported that between 1970 and 1975, 57 of the nation's 100 largest cities lost population and 43 of them gained, it was documenting the powerful and rapid shift of people away from the big cities of the North and East toward suburban areas and the warmer parts of the country.

If, in that five year period, St. Louis lost 15.6% of its population, for example, and Cleveland 14.9% and Minneapolis 13.0% and Buffalo 12.0%, there must of necessity be vacant housing units left in those cities that no well intentioned mortgage loans can save.

And when, in that same five-year period, the population of Colorado Springs rose 27.8%, and San Jose, California's rose 20.5% and El Paso, Texas' rose 19.7%, I doubt if there were many abandoned buildings in those towns even without antiredlining statutes on the books.

Experience in the "real world" has repeatedly shown that the growth or contraction of metropolitan areas is influenced by demographics, technology and patterns of income distribution, and that while government actions can speed up or slow down natural movement somewhat, they tend to have only modest long range effects on the major currents.

And sometimes governmental actions may prove counter-productive, as in the case of post World War Two highway networks and Federal housing mortgage insurance which inadvertently helped suburban areas to develop at the expense of center cities. In the case of mortgages, experience has shown that when sound underwriting standards, excellent property standards and thorough, "honest injun" appraisals are no longer required, graft, corruption and economic disaster usually follow.

The horrendous effects of well intentioned Federal Housing Authority programs 221 (d) (2) and 223 (e) (where "acceptable risk" was substituted for "economic soundness" in the spirit of the late 1960s) not only dissipated hundreds of millions of dollars of government funds, but also often led to inflated purchase prices, to blasted hopes, and, in the opinion of many observers, to foreclosures and abandonments at a rate higher than would otherwise have been the case. Anyone advocating substantial relaxation of mortgage underwriting standards should be condemned to read and reread the accounts of the FHA scandals of the early 1970s.

In the resulting foreclosures of tens of thousands of FHA-insured homes, however, the federal government could afford the financial loss; New York's banking system may not, and that is what is being proposed.

Earlier this month, when the New York City Commission on Human Rights released a 103-page report on the subject, the key recommendation was predictable; and, lo and behold, there it was, on page 11:

"All banks operating in New York State should be required to lend a fixed percentage of their assets available for investment to provide a state-administered pool of $200 million each year for the next ten years. The loans would be repaid through rents and carrying charges on the houses financed through the pool. Interest on the loans would equal the average interest rate paid by the bank to their depositors. Thus, banks would make no profit, but such a return would relieve them of any risk. (sic)"

Please note that the collateral for this $2 billion pool is to consist entirely of buildings not currently financeable through conventional means. And lest the debt service prove troublesome, the commission further suggests in the next paragraph:

"To insure that rents needed to retire the mortgages following rehabilitation will not outpace the tenants ability to pay, rent restructuring should be established at 25% of tenant income. If that amount is insufficient to retire debt service (sic), the length of the mortgage should be increased by the state."

I assume that this last thought implies 30-year mortgages for buildings with five-year life expectancies.

The article in the New York Daily News announcing this report carried the pagewide banner headline "Charge Banks' Redlining Is Ruining The City," anl the front-page story in the New York Times began with the words, "De-

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cisions about where or whether to invest in home mortgages can no longer be left to banks alone," although the story implied that the financial risks attendant on a bad guess could remain with the banks alone.

The tenor of the commission report was that "the banks" were killing various neighborhoods out of sheer cussedness. Nowhere in the 103 pages of text was there any memtion that since 1969 New York City has been losing approximately 48,000 manufacturing jobs each year, or that between 1970 and

and long term thinking brought to bear on our municipal problems. That we place a sales tax on what are already the nation's highest utility costs and insist, too on an occupancy tax on manufacturing plants while bemoaning the flight of industry is also indicative of the degree of prudence with which we are governed.

In real estate, the source of so much of the city's revenue, we find many regulations that belong more properly in "Alice in Wonderland" than in "real world" administrative codes.

A sad but representative example is the problem of getting possession of properties on which tenant leases have expired. In the case of the Shelton Hotel for example, 12 residential tenants whose leases had long run out and whose rights were solely statutory under rent control were permitted to put an entire large parcel into bankruptcy, also preventing General Telephone and Electronics Co., which employed 3,600 people, from expanding its operations in New York City. As a result, G T & E. took its future and its payroll to Stamford, Conn.

Ninety-one of New York's 125 Mitchell-Lama subsidized housing companies are in arrears on their real-estate taxes or in default on their mortgage charges for reasons that are more political than economic, and the savage discounts at which those mortgages were recently sold reflected the political realities under which we live.

The cumulative impact of these realities in recent years has been to reduce the value of property in Manhattan by some 70% in terms of the ratio of market to assessed valuation; it should not come as a surprise to find that in that period real-estate delinquencies have more than doubled and foreclosures increased fivefold.

Kenneth Patton, formerly New York's economic development administrator and currently president of the Real Estate Board, sums the problem up neatly as "a choice between the short term interests of politicians and the long term interests of their constituents."

It would be sad if the wrong choice saw New York's banking system awash in defaulted, uninsured loans and banking supervisors, like King Canute, vainly ordering the waves to go back.