



## POLICY DIRECTIONS

During the past decade, broader access to homeownership emerged as the centerpiece of federal, state, and local efforts to expand affordable housing opportunities. But just as many mortgage brokers and loan officers aggressively marketed high-risk mortgage products to vulnerable borrowers, many federal, state, and local officials also oversold the benefits of homeownership—especially to low-income and low-wealth households. The recent rise in mortgage delinquencies and foreclosures has now exposed the tragic flaw in this single-minded strategy.

Undoubtedly most Americans share the goal of becoming homeowners. Yet for many families, securing access to decent and affordable housing of any sort is even more important. What is needed is a more balanced set of policies that would expand affordable housing in both the for-rent and for-sale markets. Ironically, as the nation struggles against the fallout from the mortgage crisis, now is a good time to develop initiatives that would transform the large inventory of foreclosed properties into the next generation of affordable rental housing.

### FALLING SHORT OF NEED

At current funding levels, federal, state, and local programs serve only a fraction of the nation’s lowest-income families in desperate need. Following a rapid buildup from 1977 to 1987, growth in the number of households receiving direct assistance (public housing, housing choice vouchers, and project-based units) slowed dramatically. While the recent addition of thousands of tax-credit units helps matters, lowest-income renters often require a housing voucher to afford the rents in these units.

**FIGURE 19** Assisted Housing Covers But a Fraction of Renter Families in Need

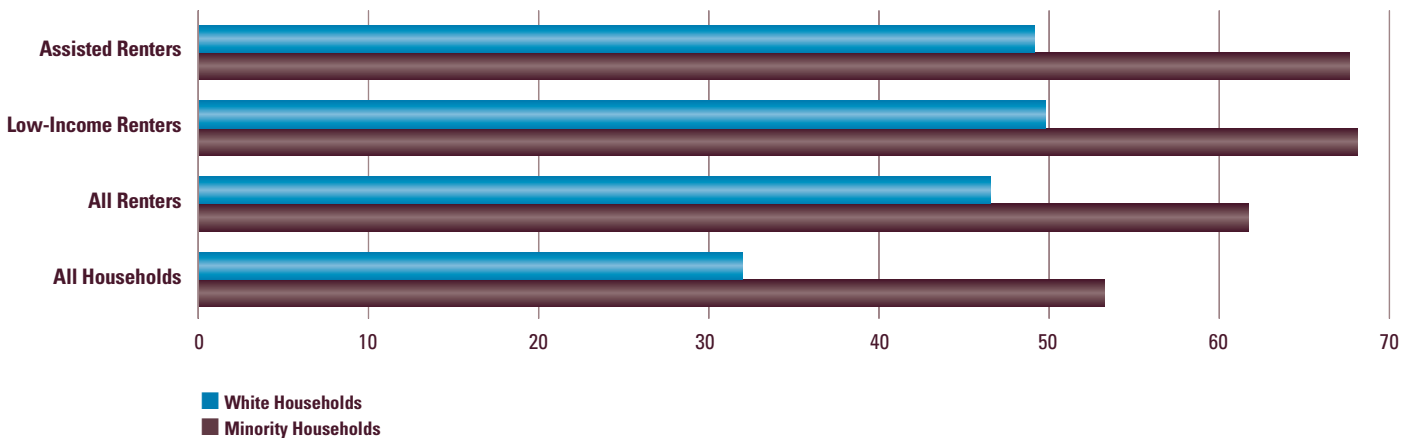
Share of Renter Households Receiving Assistance in 2005



Note: Income quartiles are equal fourths of all households, sorted by pre-tax income.  
Source: JCHS tabulations of the 2005 American Housing Survey, using JCHS adjusted weights.

**FIGURE 20****The Concentration of Assisted Renters in Center Cities Reinforces Racial Isolation**

Share of Metro Area Households Living in Center Cities (Percent)



Notes: Low-income households are in the bottom fourth of all households sorted by pre-tax income. White householders are non-Hispanic, and minority households are all others.  
 Source: JCHS tabulations of the 2005 American Housing Survey, using JCHS-adjusted weights and AHS metro definitions.

Recognizing that housing assistance is not an entitlement program, Congress has attempted to target families most in need. Lack of available assisted units, however, makes this difficult. While estimates vary, the 2005 American Housing Survey suggests that only one in five (or 6.7 million) of all renters live in assisted housing. Even among elderly renters in the lowest income quartile, less than four in ten receive housing assistance (Figure 19).

### PRESERVING AFFORDABLE UNITS

Even as new subsidized units are added—albeit slowly—to the affordable housing inventory, older subsidized units are being lost. Beginning in the late 1980s, some owners of project-based housing were able to remove their properties from the HUD-assisted inventory by prepaying their mortgages. In the mid-1990s, the trickle became a flow as the Section 8 contracts themselves began to expire and many owners opted out of the program.

Today large segments of the assisted inventory are at risk. The Government Accountability Office estimates that mortgage restrictions and rental assistance contracts on over one million subsidized units are set to expire by 2013. Efforts to encourage or force owners of assisted properties to keep their units affordable are under way, but limited funding again hampers any widespread or permanent solution.

At the same time, much of the unsubsidized but low-cost rental inventory is being lost to abandonment and demolition,

and now to foreclosure. Since developing new affordable rental housing remains difficult without steep subsidy, preserving whatever low-cost units remain should be an urgent priority. The success of preservation efforts depends in large measure on the willingness of Congress to appropriate sufficient funds to renew expiring project-based contracts and fund additional efforts to slow the loss of privately owned low-cost rentals. Without new affordable housing initiatives and expanded funding to bring these initiatives to scale, the affordable rental inventory will continue to shrink.

### REMOVING BARRIERS TO DEVELOPMENT

In addition to limited federal support, local regulations also contribute to the lack of affordable housing development. While an isolated few municipalities have taken steps to reduce or refine such regulations, many others are becoming more restrictive, either overtly or covertly. In many markets, zoning restrictions, minimum lot sizes, lengthy permitting and approval processes, and voter opposition to specific kinds of developments make the construction of affordable rental housing more difficult and therefore more expensive.

Predictably, the most restrictive municipalities have the largest shares of cost-burdened renter households. Just as predictably, low-income renters cluster in the least expensive—and often the least desirable—areas of metropolitan regions. Among all metro area households, renters are nearly twice as likely as owners to live in center city locations. The shares of low-income minority renters are even higher (Figure 20).

The concentration of lowest-income renters reflects in part the availability of assisted housing, particularly public housing. As a proportion of the metropolitan area total, over 60 percent of low-income minority renters and nearly 70 percent of assisted minority renters live in center cities.

The clustering of lowest-income and assisted renter households imposes a host of social and economic disadvantages on these groups. Among other impacts, these settlement patterns reinforce the spatial isolation of the poor, foster racial segregation, discourage investment in lower-income communities, and contribute to higher rates of crime, teen pregnancy, and school dropouts. At the same time, the lack of affordable rental housing options in job-rich environments limits the ability of lower-income families to work their way out of poverty.

### FORECLOSURES IN BOTH HOT AND COLD MARKETS

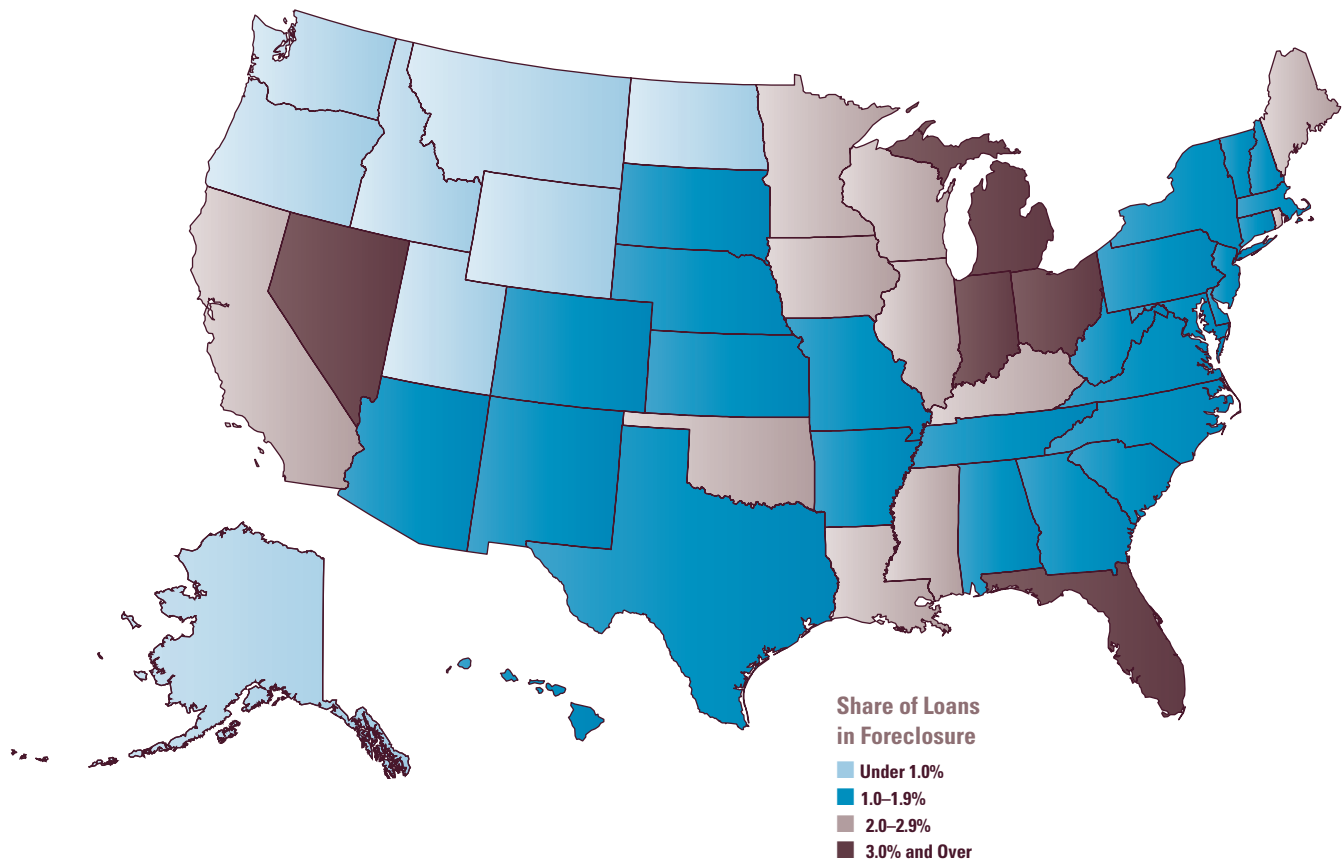
On top of the persistent problems of growing income inequality, concentration of poverty, and ongoing loss of affordable

units, the rental market disruption linked to the subprime mortgage foreclosure crisis continues to gather steam. With serious delinquencies at record levels, the Mortgage Bankers Association estimates that some 936,000 home mortgages were in foreclosure at the end of 2007. As high as this number is, it includes neither foreclosure actions that were completed earlier in the year nor the hundreds of thousands of delinquent loans that are likely to enter foreclosure in the months and years ahead.

Although the mortgage market meltdown only emerged as the dominant national housing policy issue in 2007, problems were already well entrenched in the economically distressed states of the Midwest (Figure 21). Reflecting the ongoing loss of manufacturing jobs, serious mortgage delinquencies and foreclosures have been on the rise in Ohio, Michigan, and Indiana for more than 10 years. Particularly hard hit are the center cities and the urban neighborhoods that are home to many of the region's lowest-income and/or minority renters.

**FIGURE 21** Foreclosures Are Mounting in States Across the Country

Share of Loans in Foreclosure, Year-End 2007 (Percent)



Note: Data are not seasonally adjusted.  
Source: Mortgage Bankers Association.

The recent surge in delinquencies and foreclosures in hot housing markets such as California, Nevada, and Florida—with otherwise solid income, employment, and household growth—turned a regional problem into a national one. In these states where home prices had skyrocketed, lenders aggressively marketed a set of exotic mortgage products with affordability (interest-only and payment-option) features or adjustable-rate structures with steep initial discounts. Like earlier forms of subprime mortgages, these new loan products rapidly gained market share.

Even though rising home prices added to affordability pressures in these booming housing markets, they also boosted homeowners' equity. Together with increasingly favorable financing terms, this significant equity buildup helped many overextended homeowners meet their mortgage payments simply by refinancing. For households whose incomes were growing with the overall economy, this made considerable financial sense and homeowners accumulated substantial equity by doing so.

But for others with weaker income growth, mortgage payments quickly became unmanageable. When house price appreciation eventually slowed, a growing number of households were stretched to the limit—unable to afford their current mortgages or to cover the shortfall by refinancing. The result was a sudden and dramatic jump in the number of seriously delinquent loans, as well as in the number of homeowners facing foreclosure.

#### **TOWARD A BALANCED NATIONAL HOUSING POLICY**

With foreclosures on the rise across the country, national attention rightfully focuses on efforts to help owners caught in the crossfire of the mortgage market meltdown. At the same time, it is important not to lose sight of what this housing downturn means for the rental market. Since higher-risk subprime loans are concentrated in low-income and minority communities, the fallout from foreclosures hits hardest in the areas where many of the nation's most economically vulnerable renters live.

Moreover, to the extent that mortgage market troubles have spilled over into the broader housing capital market, today's crisis will further limit the construction of affordable rental housing and add to the costs of preserving the existing lower-cost inventory. Against the backdrop of long-standing rental affordability problems and with an economic slowdown under way, now is a good time to rethink efforts to insure that all households—owners and renters alike—have access to decent and affordable housing.

For millions of American households, the overwhelming problem is not simply high housing costs, but limited income. The current focus on promoting homeownership clearly has a downside when a move from renting to owning involves swapping an unmanageable rent burden for an unmanageable mortgage burden. While many lower-income households are able to meet the high payment burdens of homeownership, many cannot. Indeed, the Homeownership Preservation Foundation reports that of the more than 80,000 distressed borrowers counseled in 2007, approximately 70 percent had incomes that were below the national median.

Although large shares of lowest-income renters face either moderate or severe housing cost burdens, over 60 percent of lowest-income homeowners also pay more than 30 percent of their meager incomes for housing (Figure 22). More than 40 percent pay more than half. Moreover, owner households in the lower-middle income quartile are more likely to face high housing cost burdens than renters with similar incomes.

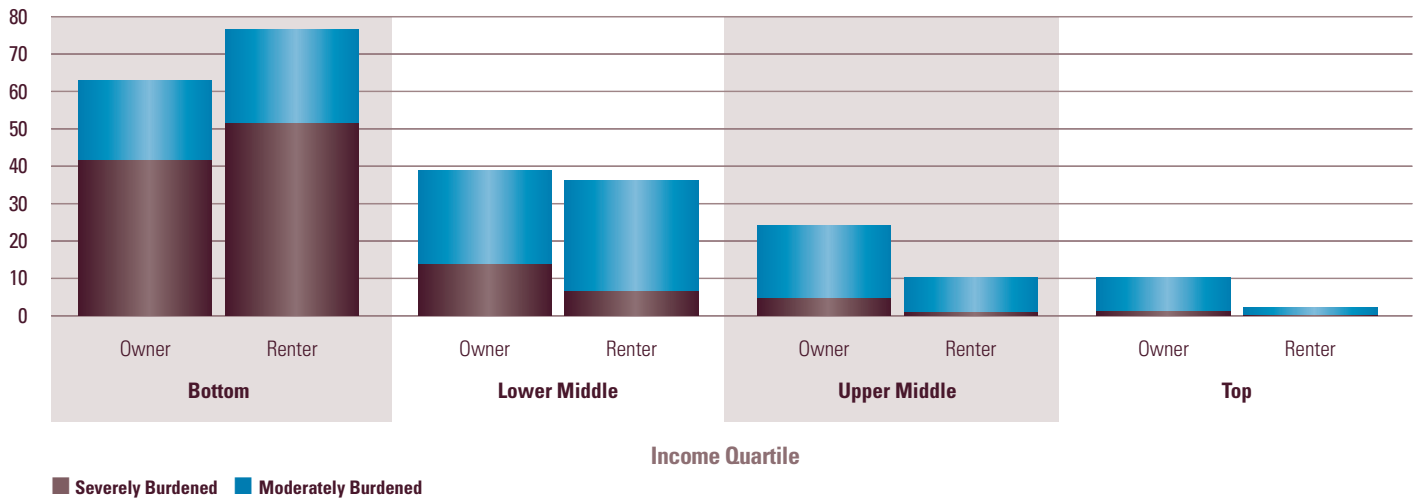
Now that large numbers of former owners are flooding back into rental markets, expanding the available supply of affordable rentals is critical. While efforts to create new units must continue, preserving the existing stock of good-quality, subsidized rental housing is even more important. In addition, recognizing that the vast majority of lowest-income renters do not live in assisted housing, it is also time to craft new programs to preserve the rapidly dwindling supply of privately owned unsubsidized rentals.

To accomplish these goals, efforts must continue to eliminate land use policies that limit development of affordable, higher-density rental housing in resource-rich suburban communities. Although regulatory reform is difficult to achieve, national housing policy must confront political opposition head on. Simply put, land use restrictions not only deter production of affordable housing, but they also promote land-intensive development that raises housing prices and imposes costs on all households, whether rich or poor, owner or renter.

Comprehensive housing assistance programs must also improve access to critical health and human services, child care, transportation, and other workforce development initiatives so that low-income and low-wealth families are able to earn decent incomes. This might involve the construction of service-enriched affordable rental housing in suburban communities as well as in inner-city neighborhoods. In this way, a balanced national policy would not only expand the range of available rental housing options, but also underpin the revitalization of distressed areas.

**FIGURE 22 Both Owners and Renters Face Affordability Constraints**

Share of Households (Percent)



Notes: Income quartiles are equal fourths of all households sorted by pre-tax income. Severely (moderately) burdened households are defined as paying more than 50% (30–50%) of income for housing.  
Source: JCHS tabulations of the 2006 American Community Survey.

Finally, access to capital is needed to support the acquisition and preservation of single-family rentals and smaller apartment buildings, including foreclosed properties now coming back on the market. On the financing side, one strategy would be to perfect pooled approaches to acquire several properties with a single financial transaction. On the equity side, new types of real estate investment trusts could be designed to raise capital from private investors to invest in smaller apartment projects. This funding would breathe new life back into the stock of older multifamily properties, which are such a crucial component of the affordable rental housing supply in many communities.

In today's soft housing market, it would also be possible to expand on this concept. As the volume of foreclosed properties mounts, many holders of these assets will be forced to sell at deep discounts. This creates an opportunity for well-capitalized players to purchase and manage distressed portfolios for a profit. What is needed is a mission-driven entity—a community preservation fund—that could participate in this market but with the goal of creating affordable housing and stable communities rather than simply maximizing profits. With skill and foresight, the nation could capture a significant share of good-quality housing at today's depressed prices to create the next generation of affordable rental housing.

A well-designed program would help lower-income owners as well as renters. For example, a publicly oriented venture could

offer more generous workout terms than presently available in the market and, in doing so, allow distressed borrowers more time to recover. Alternatively, rather than sell off foreclosed properties for the highest private return, the new entity might support a broader definition of social gain—including enhanced neighborhood stability and expanded access to affordable and sustainable homeownership opportunities.

This approach is not without risk. Managed with too much heart and too little head, this new enterprise could put millions of dollars at risk for only limited gain. But funded by some blend of public, CRA-motivated, and market-rate resources, along with earnings from the sale of performing loans and foreclosed assets, this new venture could also usher in a new era in public-private partnerships, and with it, a more balanced national housing policy.