6 HOUSING CHALLENGES

The nation has not faced housing problems of this magnitude since the Great Depression. Heavy job losses and lingering high unemployment rates have increased housing insecurity for millions of families. The share of US households with severe housing cost burdens reached a record high in 2008 and may have climbed again in 2009. Although households have switched from net spenders to savers, their balance sheets have still not recovered from the debt binge of the boom years.

WIDESPREAD COST BURDENS

After holding steady at 12 percent in both 1980 and 2000, the share of severely burdened households (spending more than half their incomes on housing) jumped by a third, to 16 percent, in 2008 **(Figure 29).** A record 18.6 million households faced these high cost burdens that year, an increase of 640,000 since 2007 and 4.7 million since 2001. Living within these households were 44.2 million Americans, including 13.7 million children.

Although the shares with cost burdens grew faster for homeowners during the 2000s, the incidence of cost burdens remained far higher for renters. Nearly one in four renter households had severe cost burdens in 2008, compared with roughly one in eight owner households. And nearly half of renters, but a third of owners, had at least moderate cost burdens (spending 30–50 percent of income for housing). The primary reason for this disparity is that renters typically have much lower incomes than owners.

The nation's 4.5 million single parents in the lowest income quartile, along with their 9.1 million children, face the worst affordability challenges. They have greater space needs and must worry more about safety and school quality when choosing homes than households without children. Half of low-income single-parent households spent 63 percent or more of their incomes on housing in 2008. Low-income minority single-parent households had even harsher cost burdens.

INCOME-HOUSING COST MISMATCH

Roughly three-fourths of households with severe housing cost burdens fall within the bottom income quartile, and a sobering half of all households in this quartile have severe burdens. This stems from a mismatch between their low incomes and the cost to supply the most basic of homes. The median income of households in the bottom quartile was $14,868 in 2008. At that level, their monthly housing costs (including utilities) would have to be no more than $372 to meet the 30-percent-of-income affordability standard. But finding even modest housing at such a low cost is next to impossible. Nowhere in the country is the HUD fair market rent for even a one-bedroom apartment at or below $372. Without government subsidies, property owners find it difficult to operate and maintain housing at such rents, let alone service debt and earn a risk-adjusted rate of return.

The long-term spread of affordability problems results from both rising housing costs and stagnating real incomes among those in the bottom quartile. A study published by the Lincoln Institute of Land Policy estimates that the real value of developed land for a single-family home nearly doubled from 1985 to 2008 in 46 studied metropolitan areas. Over the same period, the real construction cost per square foot for a single-family home was up 30 percent.

Land use and environmental regulations that restrict the supply of developable land add to housing development costs. Impact and permitting fees imposed by local governments to cover infrastructure extensions also raise development costs. At the same time, stricter building codes that dictate materials, standards, and minimum home sizes have helped to push up both the quality and the cost of housing construction.

The erosion of affordability over the last 50 years is striking **(Figure 30).** In 1960, only 12 percent of renter households spent half or more of their incomes on housing. By 2008, that share had doubled. In 1960, half of renters in the bottom income quartile spent 39 percent or less of their incomes on housing. In 2008, half spent 54 percent or more. In 1960, the median house price-to-income ratio was 1.86. In 2008, even with mortgage interest rates close to those in 1960, it was 3.34.

Of course, single-family homes are now much larger on average (2,215 sq. ft. for homes completed in 2008, compared with 1,525 sq. ft. for those completed in 1973). And the share of the housing stock with moderate to severe structural inadequacies has declined sharply (from 8.1 percent in 1989 to 5.2 percent in 2007). But in combination with slow income growth and rising land and development costs, these improvements in quality have also added to the affordability challenges of low-income households.

HOUSING COST TRADEOFFS

With long-run housing costs outpacing income growth, many Americans must make increasingly difficult tradeoffs. Those who seek to limit their expenditures can either choose lower housing and neighborhood quality in closer-in locations, or move greater distances from urban cores to take advantage of more affordable housing. They may also choose to spend less on other necessities such as food, healthcare, and savings in exchange for better housing.

In 2008, households with children in the bottom expenditure quartile that dedicated more than half their outlays to housing had less than $600 per month left for all other necessities—less than half the amount available to households with affordable housing. Similarly burdened elderly and single-person households had even less (under $500) left over after housing expenses.

But lower housing costs often mean higher travel costs and times. On average, low-income households with children that spent less than 30 percent of monthly outlays for housing devoted 4.4 times as much to transportation as those with high housing outlays. Indeed, even those households with affordable housing still had to dedicate over 37 percent of their total outlays to housing and transportation combined **(Figure 31).**

UNEMPLOYMENT AND HOUSING INSECURITY

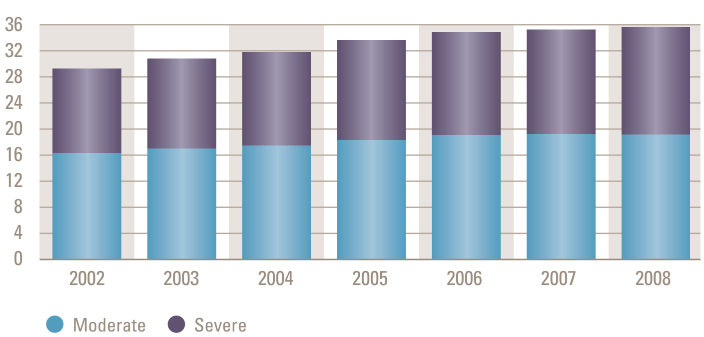
The nation lost approximately 8.4 million jobs from the beginning of the recession in December 2007 through December 2009. Under normal circumstances, the economy has to produce well over a million jobs per year to keep up with growth in the labor force. As of April 2010, the employment deficit was about 11 million. Although job growth has revived, most economists predict that it will take years to catch up and that unemployment will remain relatively high for an extended period.

Job losses and reductions in work hours have left many households with much less income to cover their housing

FIGURE 29

Affordability Problems Became Even More Pervasive After the Housing Boom Ended in 2005

Share of Households with Housing Cost Burdens (Percent)

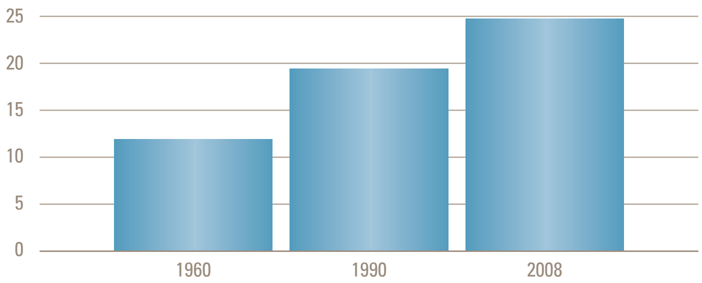


Note: Severe (moderate) housing cost burdens are more than 50% (30–50%) of pre-tax household income.
Source: JCHS tabulations of the US Census Bureau, 2002–8 American Community Surveys.

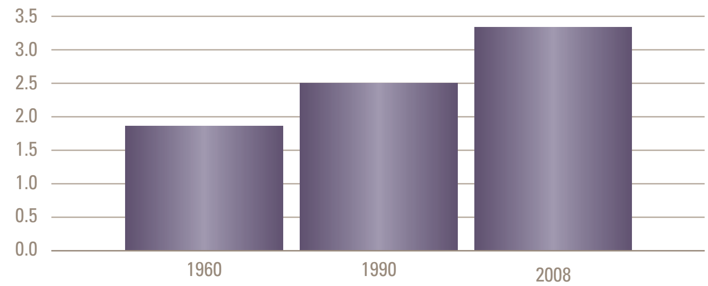
FIGURE 30

Housing Costs for Both Renters and Owners Have Risen Sharply Relative to Incomes Since 1960

Share of Renters with Severe Housing Cost Burdens (Percent)



Median Ratio of Home Value to Homeowner Income



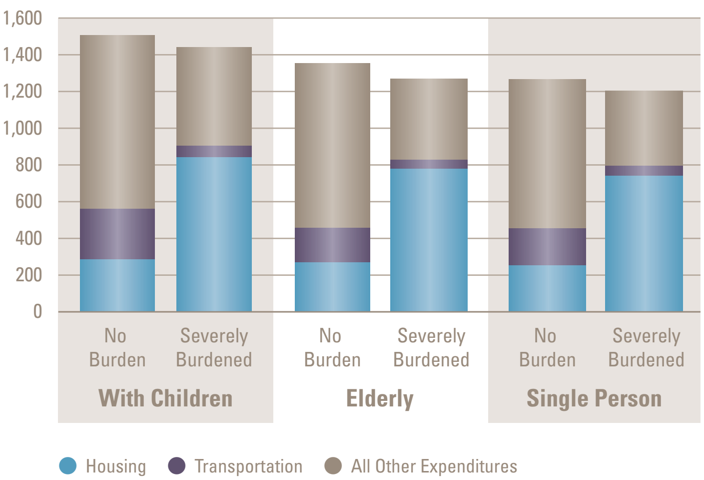
Note: Severe housing cost burdens are more than 50% of pre-tax household income.

Sources: JCHS tabulations of the IPUMS 1960 and 1990 Decennial Censuses and 2008 American Community Survey.

FIGURE 31

High Housing and Transportation Costs Limit Other Spending for Low-Income Households

Average Monthly Expenditures (Dollars)



Notes: Severely burdened (unburdened) households dedicate more than 50% (less than 30%) of monthly outlays to housing. Low-income households are in the bottom quartile of all households ranked by total monthly expenditures. Data exclude renters reporting no rental payments.

Source: JCHS tabulations of US Bureau of Labor Statistics, 2008 Consumer Expenditure Survey.

costs. Although overleveraging and overstretching income—combined with house price declines—were responsible for much of the increase in mortgage loan defaults in 2006 and 2007, joblessness is now an important driver of the foreclosure crisis. Moreover, high unemployment rates have discouraged some individuals from forming households of their own, thus slowing the absorption of vacant homes. Job losses have also kept the number of severely housing cost-burdened households high despite the improvement in affordability.

Nonetheless, the large number of multiple-earner households has helped to mitigate the effects of high unemployment. In 2009, the number of working-age households with multiple earners (39.4 million) nearly matched the number with only a single earner (39.6 million). Four-fifths of multiple-earner households fell within the upper half of the income distribution last year, providing them a larger cushion against job loss than single earners with lower average earnings have.

Despite an increase of well over a million households overall, the number of multiple-earner households dropped by 2.7 million between 2007 and 2009. At the same time, the number of households with no earners jumped by 2.2 million, or 20 percent. Some households facing short-term job losses are able to tide themselves over by collecting unemployment benefits, drawing on savings, borrowing against retirement accounts, or receiving support from family. But for others—especially households with only one worker—the impacts are immediate and disastrous. Even worse off in the current downturn are the record numbers of long-term unemployed. In April 2010, some 6.7 million workers had been out of work for more than half a year.

The groups hardest hit by unemployment are young and minority workers **(Figure 32).** Education is a key factor, with the jobless rate for workers without a high school diploma at 14.5 percent in April 2010—more than three times that of workers with college degrees. But even controlling for age and education, minorities have relatively higher unemployment rates. Moreover, there is some evidence that if a generation of young adults suffers high unemployment rates, these workers may have difficulty catching up with the incomes of preceding generations. A strong recovery could, however, give younger and minority households the lift needed to get their incomes back on track.

HOUSEHOLD DELEVERAGING

The housing boom of the 2000s triggered massive mortgage borrowing as the number of homeowners increased, the share of loans with small downpayments soared, and owners tapped into their skyrocketing home equity. Indeed, inflation-adjusted mortgage debt climbed 88 percent between the beginning of 2000 and the fourth-quarter 2007 peak.

Homeowners cashed out an astounding $1.2 trillion when refinancing prime conventional first-lien mortgages between 2003 and 2007. Some of these funds went directly to retire credit card and other nonmortgage debt, and some substituted for auto loans and other forms of consumer borrowing that might have otherwise occurred. Mortgage debt thus increased three times faster than consumer debt between 2000 and the 2007 peak.

The debt binge not only fueled consumption but also helped to inflate home prices. All told, the aggregate value of household real estate jumped 76 percent in real terms from 2000 to 2006. After the boom went bust, the value of household real estate plunged 32.6 percent from the end of 2006 through the end of 2009, while mortgage debt declined only 5.0 percent from its fourth-quarter 2007 peak.

The only ways for underwater households to reduce debt are to pay it down, have a lender agree to reduce the principal balance, have a bankruptcy judge dictate a debt reduction (though only of consumer debt, since mortgage debt cannot be "crammed down"), or lose their homes in a short sale or to foreclosure. Between 2006 and 2009, the number of bankruptcies per year climbed from 600,000 to 1.4 million, while the number of homes entering foreclosure per year (based on reports from servicers of roughly 85 percent of all mortgage loans) tripled from 800,000 to 2.4 million **(Figure 33).**

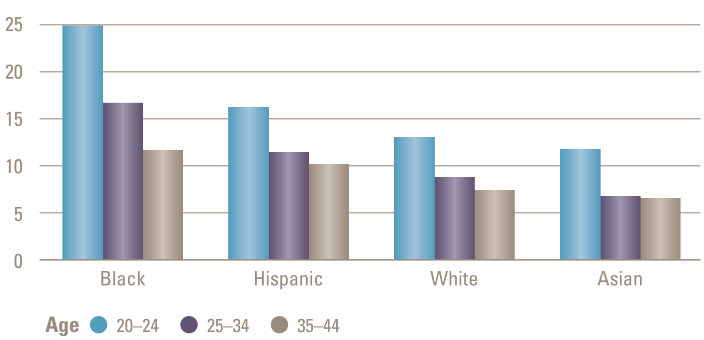
Bankruptcy has the larger negative impact on creditworthiness. VantageScore reports that individuals filing for bankruptcy with previously good ratings can lose 165–365 points from their credit scores, depending on the type of filing. Foreclosures and short sales, in contrast, reduce credit scores by a lesser but still disastrous 115–140 points. These consequences matter because credit scores govern not only the ease and cost of getting credit, but also affect renter screening and even employer hiring decisions.

Nonetheless, the overwhelming majority of borrowers who took on more mortgage and consumer debt during the boom will continue to make payments and attempt to refinance to lower interest rates. With asset values down so far, however, it may be some time before the balance sheets of these overleveraged households return to normal levels.

FIGURE 32

The Job Market Is Particularly Challenging for Young and Minority Workers

Unemployment Rate in 2009 (Percent)



Notes: Blacks, whites and Asians can be Hispanic. Hispanics can be of any race.
Source: US Bureau of Labor Statistics.

FEDERAL RESPONSES

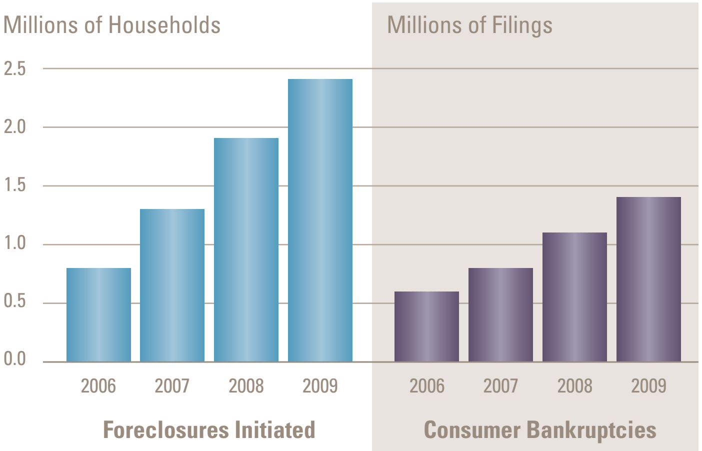
One of the most significant government programs to help forestall foreclosures and lessen housing cost burdens is unemployment insurance. States paid out $79.6 billion in unemployment benefits over the course of 2009, up from $32.4 billion in 2007. The average weekly unemployment benefit last year was $310, which for many was the only source of income. These payments enabled many families to keep their homes.

In a more direct attempt to ease the foreclosure crisis, the federal government launched the Home Affordable Modification Program (HAMP) in 2009 to reduce housing payments for eligible households to 31 percent of income for five years. While HAMP has been helpful in slowing foreclosures, it has not stopped the flood. Indeed, many of the borrowers served by the program have quickly gotten back into trouble. The US Department of Treasury expects that 40 percent of program participants will re-default.

Picking up the pieces after homes have been foreclosed thus remains a priority. The Neighborhood Stabilization Program was established in 2008 to deal with the aftermath of foreclosures. The $5.9 billion appropriated for the program is, however, small relative to the need for subsidies to acquire and rehabilitate vacant properties in poor condition in the hardest-hit communities. In many instances, governments are targeting these limited resources to a subset of the neediest neighborhoods in an effort to make a difference, even if in only a few areas.

FIGURE 33

As Households Cope with Debt and Job Losses, Foreclosures and Bankruptcies Are Soaring



Sources: Mortgage Bankers Association, National Delinquency Survey; and American Bankruptcy Institute.

Meanwhile, the financial crisis disrupted the pivotal support that state housing finance agencies (HFAs) provide to affordable rental housing and low-income homeownership programs. In late 2008, investor demand plummeted for the tax-exempt bonds that HFAs issue and the low income housing tax credits they allocate to fund these activities. The federal government countered with stopgap measures that eventually got capital flowing again, although not before a year's worth of affordable housing production was delayed and homeownership programs were interrupted. To help with local foreclosure prevention efforts, the federal government has also awarded $2.1 billion to HFAs in the five states with the steepest house price declines and an additional five states with high concentrations of unemployment.

Yet another casualty of the financial crisis is the newly created National Housing Trust Fund. Intended to support housing for extremely low-income households, this fund was to be capitalized from earnings of Fannie Mae and Freddie Mac. When the two mortgage giants went into federal conservatorship, this funding stream was suspended before it was realized. The trust now has to depend on discretionary appropriations that have yet to materialize, although the President's FY2011 budget request does include $1 billion in funding for this purpose.

Part of the federal response to the economic crisis has been to provide tax incentives for residential improvements that reduce energy consumption. This initiative not only triggered spending, but also drew attention to the tremendous savings that could be achieved through green remodeling. After adjusting for degree days, energy consumption per square foot of housing built before 1990 fell by 21.6 percent from 1993 to 2005. While in part the result of conservation, most of this decline likely reflects energy-efficient home improvements. Indeed, if all pre-2000 homes were brought up to the same efficiency level as post-2000 homes in their regions, overall residential energy consumption would fall by an additional 22.5 percent.

THE OUTLOOK

It will likely take years for the fallout from the Great Recession to abate. The 2000s ended on a sour note, with real household incomes lower than where they had started the decade and the shares of housing cost-burdened households at record highs.

With federal budget deficits looming, the resources necessary to make a noticeable dent in the nation's widespread housing affordability problems are unlikely to appear anytime soon. The share of cost-burdened homeowners may, however, ease as some stressed households default on their loans and become renters, or as others qualify for federal loan modification programs. Tighter underwriting standards and lower home prices will also keep more homebuyers from taking on excessive cost burdens right from the start.

On the rental side, the share of American households with severe cost burdens has not fallen in a meaningful way in decades, and has in fact increased. In plain terms, the cost of supplying modest units even in less desirable neighborhoods exceeds the rents that large fractions of renter households are able to pay.

In the face of these harsh realities, the Obama Administration has focused on streamlining federal housing programs and moving toward a unified scheme to peg subsidies to the fair market rent system. The government is also leveraging housing by providing some limited but path-breaking support for regional planning in coordination with the Department of Transportation and the Environmental Protection Agency. The administration has also launched the Choice Neighborhoods Initiative, designed to make transformative investments in neighborhoods where public and assisted housing is concentrated. The fate of these new programs will depend on their effectiveness and on continued funding in what will almost certainly be a difficult fiscal environment for the coming decade.