



# Executive Summary

With promising increases in home construction, sales, and prices, the housing market gained steam in early 2013. But when interest rates notched up at mid-year, momentum slowed. This moderation is likely to persist until job growth manages to lift household incomes. Even amid a broader recovery, though, many hard-hit communities still struggle and millions of households continue to pay excessive shares of income for housing.

## SINGLE-FAMILY SLOWDOWN

After kicking off 2013 on a strong note, the single-family market slowed noticeably in the second half of the year—even before the unusually harsh winter took its toll. By the first quarter of 2014, housing starts and new home sales were down by 3 percent from a year earlier while existing home sales were off by 7 percent.

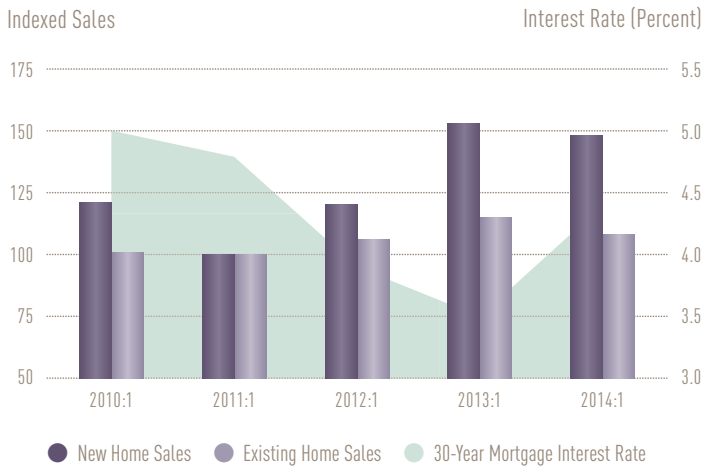
Higher mortgage interest rates were much to blame. From early 2011 to early 2013, the rate on 30-year fixed mortgages had been on a steady downtrend, sliding from about 5.0 percent to a low of 3.4 percent. This decline provided substantial stimulus to the housing market and helped to bolster the recovery that took hold in 2012. But once the Federal Reserve signaled its intent to cut back on purchases of long-term bonds and mortgage-backed securities in mid-2013, interest rates rose sharply—corresponding closely with the timing of the housing market slowdown (**Figure 1**).

Persistently low inventories of for-sale homes have been another drag on growth, with the supply of both new and existing homes holding below the six-month mark since 2012. One explanation for the limited number of homes on the market is that the share of distressed and underwater homeowners remains elevated, even though delinquency rates have fallen sharply and house price appreciation has put millions of owners back in the black. The lack of for-sale homes has also provided sellers strong bargaining power and boosted prices in most metropolitan areas, making homes less affordable. With more homes now coming on the market, though, home price appreciation is likely to moderate and sales accelerate.

Another factor in the single-family slowdown is the pullback in investor purchases of distressed properties, particularly in markets where their acquisitions are concentrated. Spurred by low home values, high rents, and limited competition from owner occupants, large institutional investors bought more than 200,000 homes as rentals in 2012 and 2013. Together with the purchases of smaller investors that had long been active in the market, these large-scale investors helped to add several million single-family rental units between 2007 and 2011. But now that the inventory of distressed homes has shrunk and single-family

FIGURE 1

### The Mid-2013 Interest Rate Jump Slowed the Recovery in Single-Family Sales



Source: JCHS tabulations of US Census Bureau, New Residential Sales; National Association of REALTORS® (NAR), Existing Home Sales; and Freddie Mac, Primary Mortgage Market Survey data.

house prices have risen, the opportunity for outsized returns in this market has diminished and investor demand has dropped.

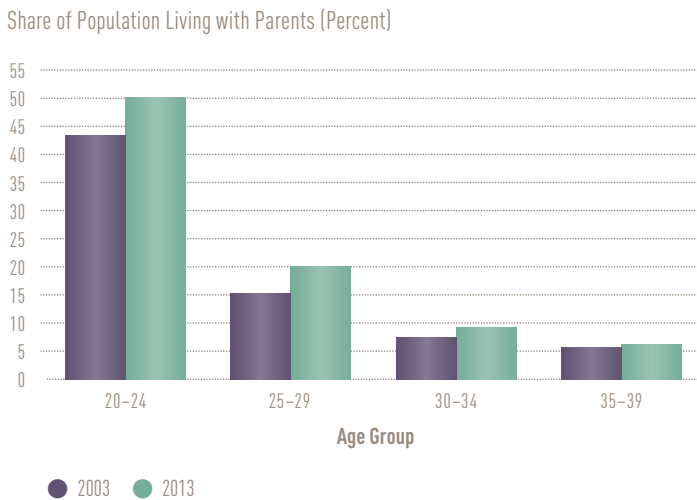
More fundamentally, though, the slow pace of the single-family housing recovery reflects steady but unspectacular job growth. Total employment has just returned to its previous peak, but remains well short of the gains necessary to accommodate the several million additional working-age adults that have joined the labor force since the start of the recession. As long as employment gains remain steady but modest, the pace of the housing recovery is likely to follow suit.

#### LONGER-TERM DEMAND

While the major household surveys offer conflicting views, it seems clear that household growth remained subdued in 2013 despite the improving labor market and the coming of age of the large millennial generation. Much of the sluggishness of household growth in fact relates to lower headship rates among this age group—driven not only by a slowdown in immigration but also by the increasing share that continue to live in their parents' homes. Indeed, some 2.1 million more adults in their 20s and 300,000 more adults in their 30s lived with their parents in 2013 than if the shares living at home had remained at 2007 levels.

FIGURE 2

### Despite Recent Increases, the Shares of Younger Adults Living with Parents Are Still Likely to Drop Sharply with Age



Source: JCHS tabulations of US Census Bureau, Current Population Surveys.

The fact that these delayed moves have held back household growth in recent years has fed hopes that the housing market recovery would accelerate once employment growth revived and younger adults were able to get jobs. This rebound has yet to occur, even though many living at home are now employed. Historically, however, the share of adults living with their parents drops sharply after age 24 and continues to fall to 6 percent by the mid- to late 30s (**Figure 2**). Regardless of the economic setbacks they may have experienced, today's 20–29 year olds are still likely to follow the same pattern. Assuming current headship rates hold, the number of households in their 30s should therefore increase by 2.7 million over the next decade and provide a strong lift to the rental and starter home markets.

Many of tomorrow's younger households will be minorities (**Figure 3**). By 2025, minorities will make up 36 percent of all US households and 46 percent of those aged 25–34, thus accounting for nearly half of the typical first-time home-buyer market. Since minority households tend to have lower incomes and wealth than white households, their demand for owner-occupied housing will depend in large measure on the availability of mortgage financing that accommodates their limited resources.

Meanwhile, the aging of the baby-boom generation over the next decade will lift the number of households aged 65 and over by some 10.7 million. Many of these households will choose to make improvements and modifications to their current homes so that they can age in place, while others will seek out new housing options geared toward seniors.

Given the current size of the adult population as well as current headship rates by age or race/ethnicity, the Joint Center for Housing Studies estimates that demographic trends alone will push household growth in 2015–25 somewhere between 11.6 million and 13.2 million, depending on foreign immigration. This pace of growth is in line with annual averages in the 1980s, 1990s, and 2000s, and should therefore support similar levels of housing construction as in those decades.

### STABILIZING HOMEOWNERSHIP RATES

The US homeownership rate declined for the ninth consecutive year in 2013. According to the Housing Vacancy Survey (HVS), the national rate stood at 65.1 percent—its lowest reading since 1995. But even though the number of owners was still falling last year, the decline was the smallest posted since 2008.

Indeed, many of the conditions holding the owner-occupied housing market back continue to improve. Steady employment growth will give more potential homeowners the ability to buy, while rising home values will encourage more households to act on that ability before prices climb even further. The share of distressed homeowners is also on the decline, reducing the number of households forced to move out of homeownership.

In the near term, though, the homebuying market still faces a number of headwinds. Higher home prices and interest rates have made homeownership more of a financial stretch for many households. The National Association of REALTORS® (NAR) reports that the median home price climbed 10 percent year over year in

December 2013 and the interest rate on a 30-year fixed mortgage was up by nearly a full percentage point. As a result, the monthly payment for the median-priced home jumped 23 percent in just one year. Higher FHA mortgage insurance premiums make the increase even larger for borrowers making low downpayments.

Falling incomes are also taking their toll. Between 2007 and 2012, real median household incomes dropped 8 percent among 25–34 year olds and 7 percent among 35–44 year olds (**Figure 4**). For the past two decades, homeownership rates for both of these age groups have closely tracked changes in incomes, rising through the 1990s before turning down in the middle of the 2000s. However, the economic recovery may have advanced enough to allow growth to resume, with 2012 incomes edging up 1.2 percent among workers aged 35–44 and dipping just 0.3 percent among those aged 25–34.

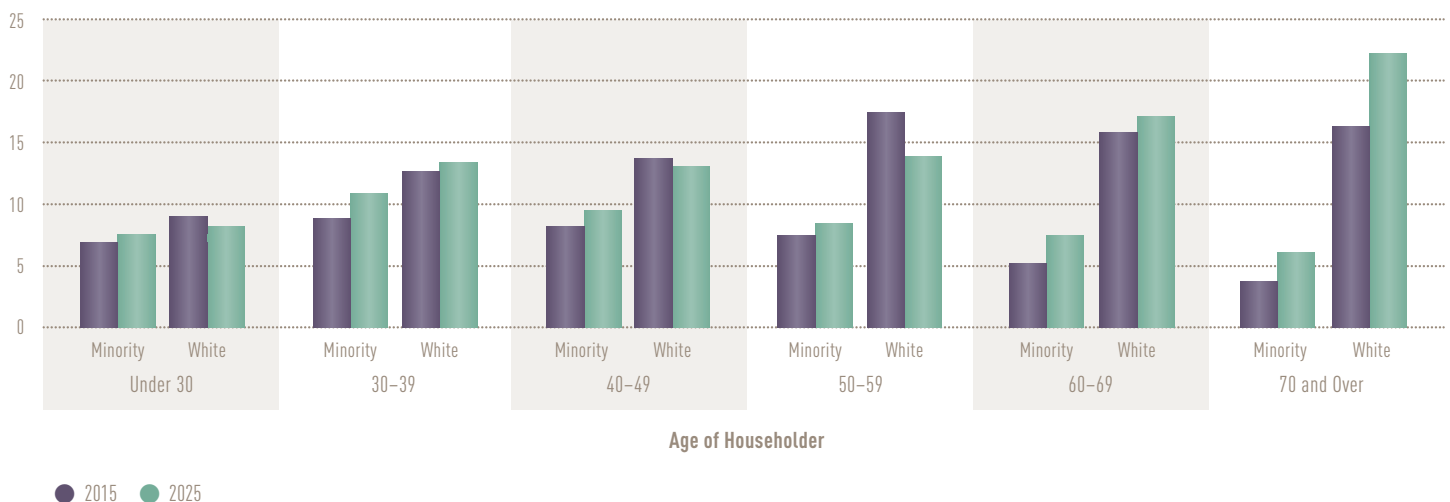
In addition, many would-be homebuyers may be burdened by student loan debt. Between 2001 and 2010, the share of households aged 25–34 with student loan debt soared from 26 percent to 39 percent, with the median amount rising from \$10,000 to \$15,000 in real terms. Within this group, the share with at least \$50,000 in student debt more than tripled from 5 percent to 16 percent. For these borrowers, the need to pay off these outsized loans will likely delay any move to homeownership.

Adding to these financial pressures, qualifying for mortgage loans is still a challenge—especially for those with lower credit scores. Indeed, the average score for Fannie Mae-backed mortgages rose from 694 in 2007 to 751 in 2013. The increase for

FIGURE 3

### Younger Minorities and Aging Baby Boomers Will Drive Household Growth Over the Coming Decade

Projected Households (Millions)



Source: JCHS 2013 middle-series household projections.

FHA loans, from 640 to 693, was even larger not only because lending to applicants with scores below 620 essentially stopped, but also because many borrowers with relatively high scores turned to FHA after failing to qualify for conventional mortgages. While some lenders have announced that they are ready to relax underwriting standards, it is too soon to tell how large an impact this will have. An easing of credit constraints will be one of the most important determinants of how strongly the national homeownership rate rebounds in the coming years.

#### CONTINUING RENTAL MARKET STRENGTH

While slowing, growth in the number of renter households was still on the rise last year. The CPS reports the addition of more than one million new renters annually between the 2005 peak in homeownership and 2013—double the average pace in any decade since the 1960s. Although the HVS estimate is much lower, both surveys indicate that renter household growth remains above long-run averages.

On the strength of this demand, vacancy rates continued to fall and rents continued to rise nationally as well as in many metropolitan areas across the country. According to MPF Research, rents for professionally managed apartments climbed 3 percent in 2013. Meanwhile, increases in the 20 most rapidly appreciating rental markets averaged 6 percent, up from 5 percent in 2012. While many of these hot markets are in northern California, the list also includes Corpus Christi, Denver, and Fort Myers.

The ramp-up in multifamily construction also continued in 2013, with starts increasing 25 percent and surpassing the 300,000 mark for the first time since 2007. The number of new multifamily units intended as rentals was also at its highest level since 1998. Construction in nearly half of the top 100 metros is back to average 2000s levels, and has approached or exceeded previous peaks in a handful of markets that include Austin, San Jose, and Washington, DC. At the same time, though, rental construction in areas that experienced the sharpest building booms and busts remains depressed.

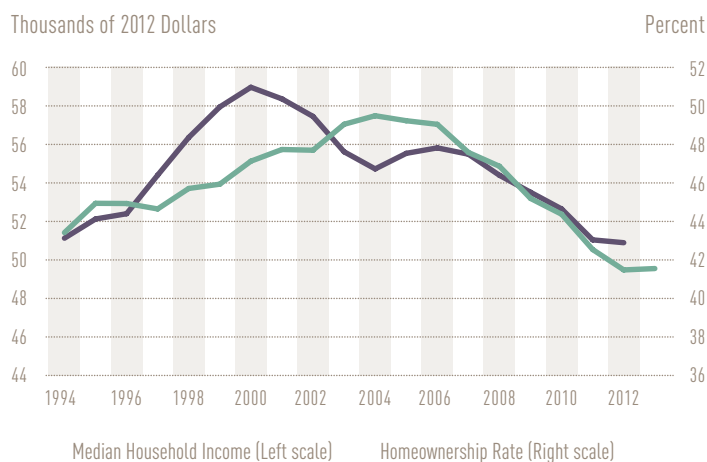
Demand and supply appear to be near balance (**Figure 5**). MPF Research data indicate that the number of occupied apartments in investment-grade properties increased by more than 200,000 annually from 2010 through early 2012. Over the same period, additions to the supply were well below that level, helping to bring down vacancy rates and lift rents. As of the last quarter of 2013, however, slower growth in occupied apartments and faster growth in new apartments coming onto the market brought these measures into alignment.

Meanwhile, the multifamily property market is flourishing. According to Moody's/RCA Commercial Property Price Index, property values increased by double digits for the fourth consecutive year in 2013, pushing values above their previous peak. Delinquency rates have also declined substantially in all market segments, although the rate among loans held in commercial mortgage backed securities remains relatively high. Amid these improving conditions, banks and thrifts raised their multifamily

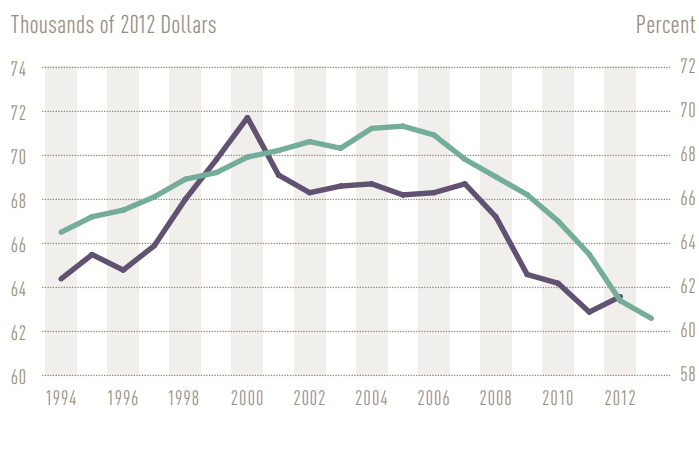
FIGURE 4

### The Rise and Fall in Homeownership Among Younger Households Mirrors Income Trends

#### 25–34 Year Olds



#### 35–44 Year Olds

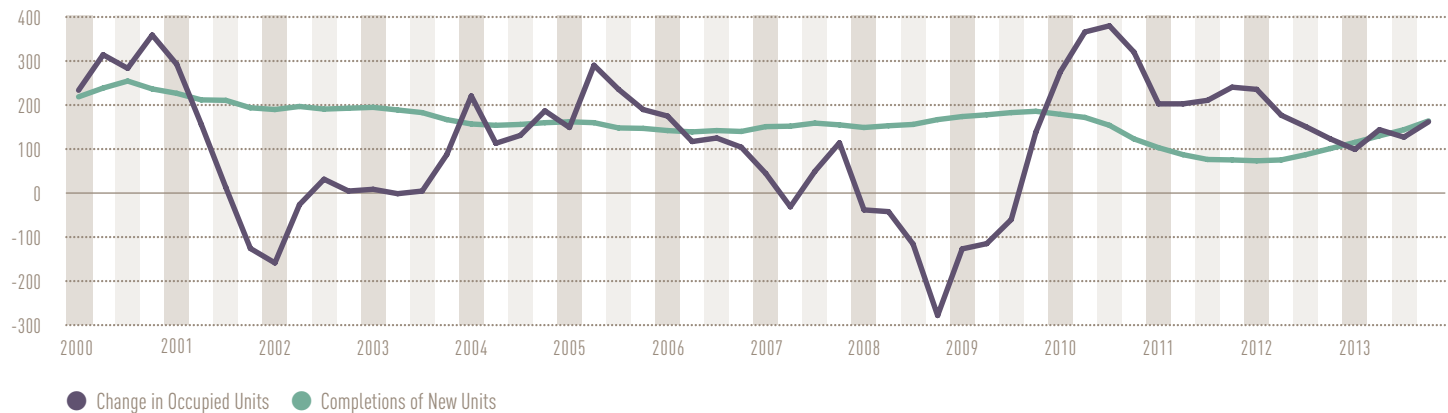


Notes: Incomes are adjusted for inflation using the CPI-U for All Items. Incomes for 2013 are not yet available.  
Source: JCHS tabulations of US Census Bureau, Housing Vacancy Surveys and Current Population Surveys.

FIGURE 5

## Multifamily Rental Supply and Demand Returned to Balance in 2013

Units (Thousands)



Notes: Data cover investment-grade multifamily properties. Changes in occupied units and completions of new units are four-quarter totals.  
Source: JCHS tabulations of MPF Research data.

mortgage holdings by \$29 billion in 2013—more than twice the growth in government-backed loans.

### THE STRETCH TO AFFORD HOUSING

Based on the traditional affordability standard (housing costs of no more than 30 percent of income), more than a third of US households live in housing that exceeds their means. Indeed, the share of cost-burdened households rose steadily from 29.6 percent in 2001 to a record 37.2 percent in 2010, before retreating to 35.3 percent in 2012 (**Figure 6**).

For renters, this is indeed a crisis of affordability. The share of cost-burdened renters increased in all but one year from 2001 to 2011, to just above 50 percent. More than a quarter of renter households (28 percent) had severe burdens (paid more than half their incomes for housing). In 2012, the share of cost-burdened renters improved slightly but their numbers held steady as more households entered the rental market.

On the homeowner side, the share with cost burdens crested in 2008 at 30.4 percent, up 6 percentage points from 2001. The share then held steady for several years before edging down in 2011. Much of this improvement reflects the fact that many owners were able to refinance their mortgages at much lower interest rates. More important, though, the number of owners with mortgages fell by 2.7 million in 2007–12 as the foreclosure crisis progressed, matching the drop in the number of mortgaged owners with cost burdens. Moreover, even after two years of declines, the share of cost-burdened homeowners stands well above levels at the start of the last decade.

Lower-income households are especially likely to be cost burdened. Among those earning less than \$15,000 a year (roughly equivalent to working year-round at the federal minimum wage), 82 percent paid more than 30 percent of income for housing in 2012 while 69 percent paid more than half. Although conditions among households making \$15,000–29,999 are slightly better, the share with at least moderate cost burdens was 64 percent and that with severe cost burdens was 30 percent.

The inability to find units they can afford forces many households to sacrifice on housing quality and/or location. Even with these tradeoffs, though, housing costs often exceed their ability to pay and thus result in limited spending on other necessities. Compared with households living in affordable housing, severely cost-burdened households in the bottom expenditure quartile (a proxy for low income) spend 39 percent less each month on food and 65 percent less on healthcare. These cutbacks seriously undermine the basic well-being of low-income households.

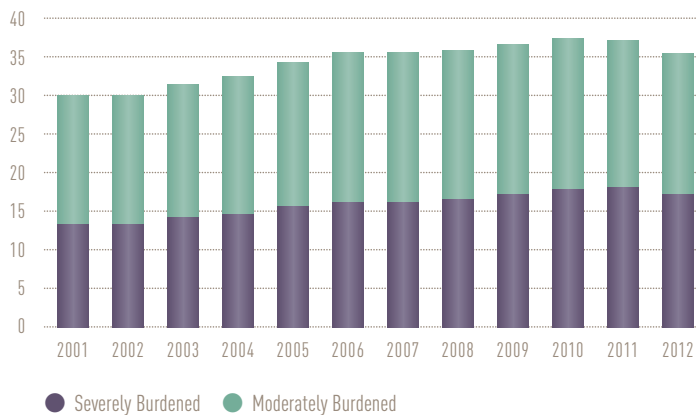
Living in inadequate housing presents additional hazards to health and safety. In 2011, the American Housing Survey found that extremely low-income households (earning less than 30 percent of area medians) were more than three times more likely to live in structurally deficient units as households earning at least 80 percent of area medians. Moreover, lowest-income households opting for housing they could afford were 43 percent more likely to live in inadequate units, underscoring the tradeoff between affordability and quality.

When available, federal rental subsidies thus make a fundamental difference in quality of life for these families and individu-

FIGURE 6a

## Despite a Small Improvement in 2012, Housing Cost Burdens Are Still Widespread...

Share of Households (Percent)



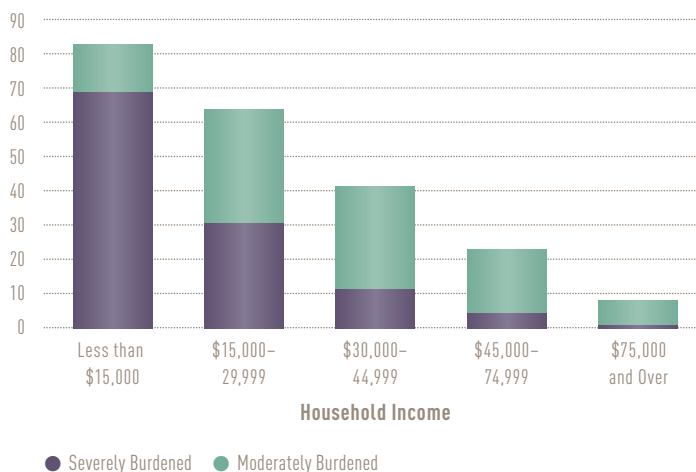
Notes: Moderately (severely) cost burdened is defined as paying 30–50% (more than 50%) of income for housing. Households with zero or negative income are assumed to be severely burdened, while renters paying no cash rent are assumed to be without burdens.

Source: JCHS tabulations of US Census Bureau, American Community Surveys.

FIGURE 6b

## ...Particularly Among Lower-Income Households

Share of Households (Percent)



Notes: Moderately (severely) cost burdened is defined as paying 30–50% (more than 50%) of income for housing. Households with zero or negative income are assumed to be severely burdened, while renters paying no cash rent are assumed to be without burdens.

Source: JCHS tabulations of US Census Bureau, 2012 American Community Survey data.

als. But between 2007 and 2011, the number of income-eligible renters rose by 3.3 million while the number of assisted housing units was essentially unchanged. Sequestration forced further cuts in housing assistance, which President Obama's FY2015 budget proposal attempts to reverse. But even if that increase occurred, securing housing assistance is increasingly difficult. At last count in 2011, more than three-quarters of low-income households that qualified for subsidies were left to find housing in the private market. For the nation's 11.5 million extremely low-income renters, this meant competing for a dwindling stock of just 3.2 million units that were both affordable and available.

### LOOKING AHEAD

Despite their rebound in the last two years, home sales and starts are still nowhere near normal levels. Indeed, single-family construction is running below rates hit during the depths of the 1980–82 recession. But if income and employment trends continue, household growth—especially among younger adults—should also pick up and thus help to support demand for both rental and owner-occupied housing.

The future course of homeownership will depend largely on the cost and availability of mortgage financing. On the private side, looser mortgage underwriting standards may help to bolster the housing market recovery. On the government side, with no mortgage market overhaul in sight, Fannie Mae and Freddie Mac—along with FHA—will continue to shape conditions in the short to medium term. After sharply raising their guarantee fees and insurance premiums in recent years, all three entities are taking steps to buoy the homebuying market. For example, FHA recently introduced a counseling-based program that provides borrowers an option to lower their premiums. Federal agencies are also working to expand access to mortgage credit by convincing lenders that they can extend well-documented loans to lower-credit-score borrowers without fear of reprisal in the case of default.

Meanwhile, prospects for improving rental housing affordability are bleak. While a pickup in income growth and an easing in rents would help to reduce the alarmingly high number of cost-burdened renters, the cost of market-rate housing will still be out of reach for many. For these households to have the stability they need to seek opportunity, rental assistance is the only option. Without expanded federal funding to aid the neediest households, millions of US families and individuals will continue to live in housing that they cannot afford or that is inadequate, or both.