CALIFORNIA DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

State of California – Business, Transportation and Housing Agency - Edmund G. Brown Jr. Governor

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The State of Housing in California 2012: Affordability Worsens, Supply Problems Remain

California's housing market ended on a stronger note in 2011 and shows signs of improvement for 2012. A robust recovery is not forecast until 2013.[1] Despite six years of decline in housing prices, the State still lacks an adequate supply and mix of housing, in the right locations, and affordable to families, the workforce and special needs populations. Furthermore, the affordability of rental housing in many markets has gradually deteriorated due to falling incomes and rising rents. Regarding affordability of ownership housing, financing remains difficult for many due to tight lending requirements.

Prior to the foreclosure crisis and current economic downturn, frequently referred to as the Great Recession, California had experienced decades of undersupply, contributing to significant price escalation and worsening affordability. The University of Southern California (USC) Population Dynamics Research Group found that while the recession of the early 1990s was most devastating with regard to poverty and unemployment, the housing price declines, construction downturn, and foreclosures have been worse in the Great Recession of the mid-2000s.

"We expect a modest growth in housing starts for the balance of the year at approximately one quarter of the U.S. rate… predominantly multi-family housing. In 2013, we forecast a 40% jump in permits, slightly above the U.S. rate and a dramatic rise to 130,000 permits in 2014, double the U.S. rate."

Jerry Nickelsburg, Senior Economist, UCLA Anderson Forecast, June 2012

This recession worsened the effect of long term inadequate supply and affordability problems and has not been offset by vacant units resulting from foreclosures, or from depressed market conditions. While the housing market is stabilizing, its recovery may be different from previous crises and is being shaped by new market conditions and shifting trends. Without fail, the supply and affordability issues are present more than ever.

This paper highlights the State's demographic trends and factors contributing to California's continuing housing supply shortage and affordability problems.

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[1] UCLA Anderson Forecast for California. June 2012. "*California Housing Market: Data, Mirages and Recovery*"

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Contents

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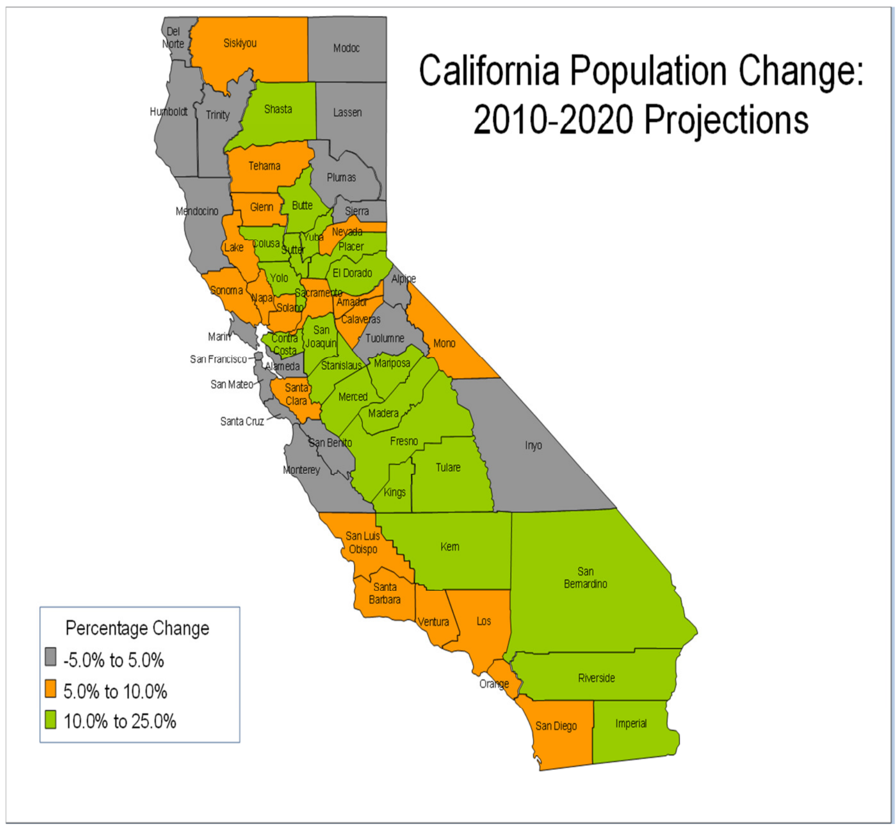
I. Demographics

California continues to experience steady and diverse population growth

Despite the recession in the early 1990s and the continuing market downturn, California's population has still grown by approximately 340,000 people annually since 2000. Somewhat slow by historical California standards, this annual growth amounts to the second largest numerical increase in a U.S. state's population over the past decade. California is projected to experience continuing steady, homegrown population gains from within the State over the next decade, considered to be at "normal" levels.[2] Despite the current market crisis, Californians continue to form households, have children, expand their families and live longer! Even with immigration slowing down, the State demographic composition has already been shaped: California is steadily becoming more diverse, with a majority of its population Californian-born, for the first time since the Gold Rush.[3]



Source: State of California, Department of Finance, Interim Population Projections for California and Its Counties 2010-2050, May 2012

The 2010 Census revealed the most significant growth occurred in the Hispanic and Asian populations, at 28 percent and over 31 percent, respectively, a trend that is likely to continue in the coming decade. The Department of Finance projects that while the Non-Hispanic White group will grow less than one percent by 2020, the Hispanic group is projected to grow by 21 percent, and the Asian group by 11 percent. Geographically, inland areas will experience particularly high growth rates.

Demographers recognize another significant trend: the growing dominance of homegrown Californians, with 98 percent of the projected growth being comprised of native-born children of immigrants reaching majority for the first time in 2010, and projected to continue to rise over the next two decades. This young, diverse and prominently homegrown generation, being the future driver in the housing market and pool of homebuyers, will provide an advantage over other states with aging population.[3,4]

[2] State of California, Department of Finance, *Interim Population Projections for California and Its Counties 2010-2050*, Sacramento, California, May 2012. http://www.dof.ca.gov/research/demographic/reports/projections/interim/view.php
[3] Myers, Dowell, July 2012 "California Futures: A Changing Society Needs New Narratives". http://www.usc.edu/schools/price/research/popdynamics/pdf/2012_Myers_CaliforniaFutures_Boom.pdf
[4] John Pitkin and Dowell Myers. 2012. "*Generational Projections of the California Population by Nativity and Year of Immigrant Arrival*". Produced by the Population Dynamics Research Group, Sol Price School of Public Policy, University of Southern California. http://www.usc.edu/schools/price/research/popdynamics

These demographic trends play a central role in fueling steady and diverse future housing demand. As ethnic and racial groups form households in a different manner than white non-Hispanics, the housing demand that they trigger in the near future may diverge from last decade's conventional demand. For example, Hispanic households tend to have more children and are more likely to include multiple generations in their households, thus creating demand for larger homes accommodating extended families.

Preference for location of housing may also be influenced by these demographic trends. Pitkin and Myers found in a recent study that Hispanic households remain much more likely to locate in central cities and metropolitan areas than non-Hispanic households. Housing preferences of households with foreign-born householders – an important subset of these ethnic and racial groups, are substantially different from those of native-born, as these households are more likely to choose higher densities and multifamily structures. These differences tend to level off with time due to assimilation.[5]

The mix of preferences and needs of the State's diverse population will be drivers for more diverse housing demand in decades to come.

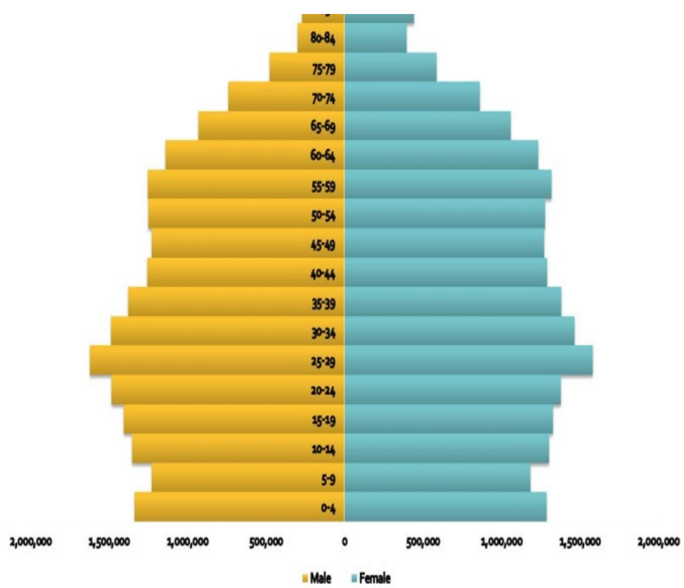
The greatest growth is projected for aging baby-boomers (55+) followed by generation Y (25-34)

The Urban Land Institute summarized in a 2010 study four large demographic groups facing a unique set of challenges, and driving the housing markets for the next decade:

- Older baby boomers, who will live longer than previous generations and constitute a senior population unprecedented in size;
- Younger baby boomers, many of whom may be unable to sell their current suburban homes to move to new jobs;
- Generation Y, which will be renting housing far longer than they did in past generations, partly because of high college debt;
- Immigrants and their children, who will want to move to the suburbs but may find housing there too expensive, even after the current drop in prices.[6]

These trends are dramatically different from the past decade and, combined with the shifts in ethnic and racial composition of population growth, can substantially affect the type and location of housing demand throughout California.

California Projected 2020 Population by Gender and Age Group



Source: DOF Interim Projections 2020. July 2012

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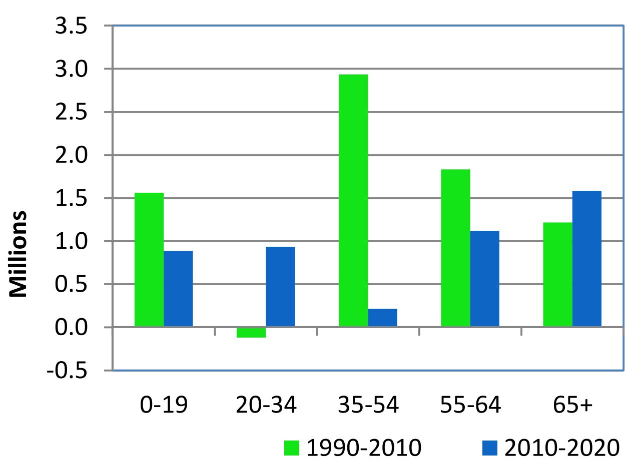
[5] Pitkin, John and Myers, Dowell *"U.S. Housing Trends: Generational Changes and the Outlook to 2050"*; Prepared for Transportation Research Board, National Academy of Sciences, Washington, D.C., May 2008

[6] John McIlwain, Urban Land Institute, *"Housing America. The Next Decade"* http://www.uli.org/~/media/Documents/ResearchAndPublications/Fellows/McIlwain/HousinginAmerica.ashx

Currently the sixth youngest state, California will soon begin aging faster than the nation, as the number of Californians 65 and older will double over the next twenty years, from 4.3 million in 2010 to 8.4 million in 2030.[7] Observing the characteristics of the aging population is instrumental in understanding housing demand. Older Californians usually have the highest housing demand per 1,000 people – the result of divorces, separations and deaths. The Department of Aging indicates that one in five elderly (over 60 years old) live alone.[8] An overwhelming percentage of the elderly (88 percent per a recent AARP survey) prefer to age in place because of affordability issues and ability to remain independent. A 2009 survey by real estate advisory firm Robert Charles Lesser and Co.(RCLCO) found that 75 percent of retiring boomers want to live in mixed-age and mixed-use communities, and more urban settings. Baby–boomers are projected to dominate changes in the housing market until at least 2030, with their preference for aging in place, or strong demand for active living housing, near transit and services, or need for assisted living.[9]

Complementing and nearly outnumbering the aging population is the echo-boomer generation which is more diverse, and entering household formation ages. The RCLCO's 2008 survey found that 77 percent of this generation reports wanting to live in an urban core, rather than the suburbs where they grew up, and are willing to live in smaller places to be able to afford their lifestyle.

1990 - 2020 Changing Housing Demand



Source: S. Levy, *California's Changing Demography: Implications for Housing* Presentation, May 2011, USC

This younger generation may augment the demand for apartments and smaller starter homes in urban centers over the next decade.[10]

As such, an increase in one-person and older households is likely to continue for the next several decades, driving the need for more housing and different housing products. By 2030, one in four homes is projected to be occupied by a single-person,[11] while a growing number of homes will be occupied by empty-nesters or households without children.

At the other end of the spectrum is the preference for larger housing units accommodating multigenerational households which may be amplified by weak economic conditions. The number of households in which two-three generations live together (adults, elderly parents, or grown children) has spiked in the past five years, as the economic conditions forced many families to change their living arrangements. Between 2007 and 2009, the number of multi-generational households in the nation increased by 10.5 percent. Demographers predict multigenerational households will continue

[7] Hayutin, Adele, Stanford Center for Longevity. 2012. *"California's Aging Population: Not Forever Young"*. http://longevity.stanford.edu/blog/2012/06/californias-aging-population-not-forever-young/

[8] California Department of Aging. 2012.http://www.aging.ca.gov/Data_and_Statistics/

[9] Myers, Dowell and Ryu, SungHo, "*Aging Baby Boomers and the Generational Housing Bubble: Foresight and Mitigation of an Epic Transition*", 2007, Journal of the American Planning Association, 74:1 http://dx.doi.org/10.1080/01944360701802002

[10] Joint Center for Housing Studies of Harvard University, *"State of the Nation's Housing 2010",* p .14 http://www.jchs.harvard.edu/publications/markets/son2010/son2010.pdf

[11] Arthur Nelson "*America Circa 2030: The Boom To Come",* Architect Magazine, October 15, 2006. http://www.architectmagazine.com/retail-projects/america-circa-2030-the-boom-to-come.aspx

to rise as baby boomers seek care with family members, children affected by the slow job market boomerang home, or delay leaving their parents' home, and as ethnic or racial groups more likely to live with extended family continue to grow. In response to these trends, the housing industry features new concepts of housing type enabling extended families to stay close together while retaining independence.[12]

Given the variety of housing preferences and needs of the State's diverse population, an assortment of rental and owner options are needed to accommodate households in different stages of life and for all income levels. These trends combined will likely result in a stronger demand for a variety of housing types located in denser, more urban settings, closer to services and amenities.

[12] Amy Taxin, Huffington Post. April 2012. *"Builders Revamp Home Design To Accommodate To Multigenerational Families"* http://www.huffingtonpost.com/2012/04/16/home-designs-accomodate-multigenerational-families_n_1428493.html

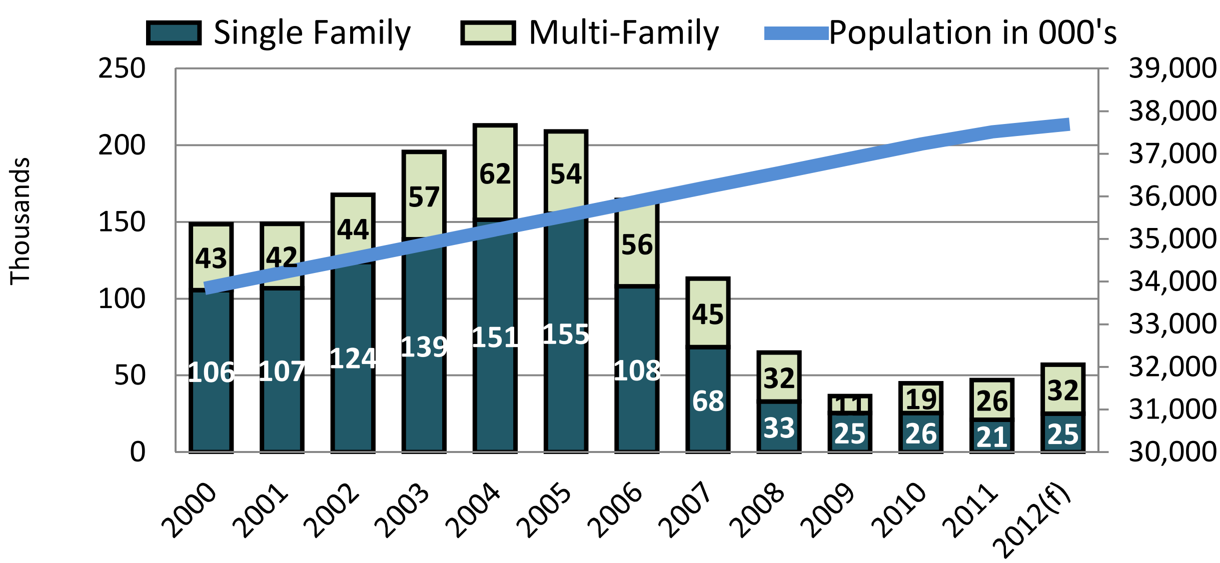
II. Housing Supply

New home construction stabilizing in 2012, but still slow to rebound

A recent study depicting construction trends in California since 1960 shows dramatic fluctuations in number of permits in the past that closely follows business cycles.[13] The 1990 recession involved a prolonged downturn, with six years of depressed construction followed by a surge in construction that continued into the next decade.

California was already behind in meeting its housing need relative to population and employment growth when residential permits in the last decade peaked in 2004 at over 212,960. Just when residential construction was approaching the average annual need to accommodate the State's population growth and mobility, the bottom fell out of the financial sector with the foreclosure crisis and recession. During the past decade, residential new construction has averaged less than 150,000 permits per year, lagging well behind the State's annual average need.

California Population Growth and
New Housing Permits 2000 - 2012



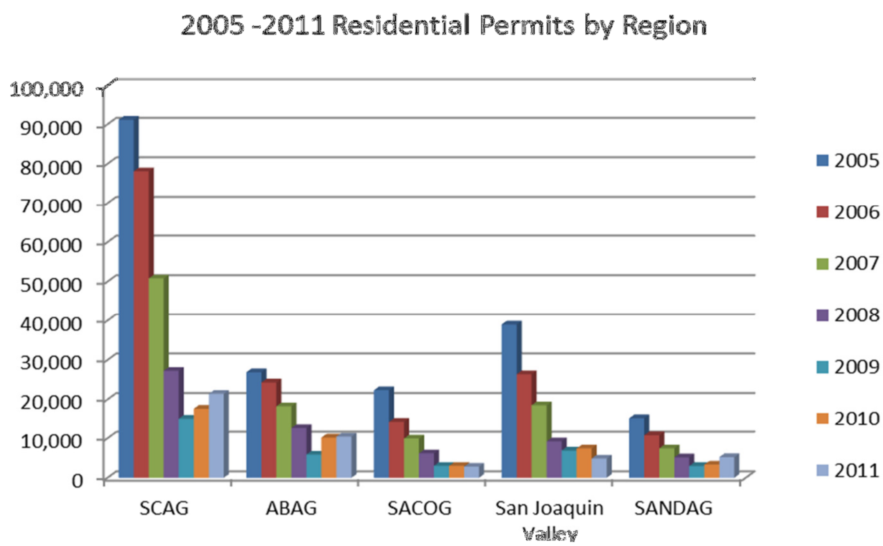
Source: Construction Industry Research Board/California Homebuilding Foundation and DOF. 2012

Residential permits spiraled down in 2009 to just over 35,000 (approximating a 84 percent decrease from 2004), the lowest level of permits in 55 years of historical records. Multifamily permits decreased by 80 percent, from 62,000 in 2004 to just over 11,000 in 2009.[14] During 2011 housing production has continued to lag at 47,171 permits, less than a quarter of the 2004 peak level. During the first quarter

[13] Dowell Myers, Ray Calnan, Anna Jacobsen and Josh Wheeler, *"California Roller Coaster-Income and Housing in Boom and Bust, 1990-2010"*April 2011 and July 2012 Update, sponsored by the John Randolph and Dora Haynes Foundation, p.7 http://www.usc.edu/schools/sppd/research/popdynamics/pdf/2011_Myers-etal_California-Roller-Coaster.pdf

[14] Construction Industry Research Board (CIRB), *California Construction Review*, Burbank, April 2011

of 2012, homebuilding reached a four-year high, rising on a wave of new apartment construction.[15] Of the 12,000 residential permits issued in the first quarter of 2012, 7,000 or approximately 60 percent were multifamily permits. While the number of permits varies significantly by region, the proportion of multifamily permits statewide increased in all regions from 2009 to 2011.



Source: Construction Industry Research Board. 2011

Current 2012 forecasts do not predict recovery until 2013.[16] In 2012, residential permits are forecasted to reach 57,000, 20 percent more than 2011, still only roughly a quarter of the 2004 peak. This prolonged vacillation in new housing construction continues to deepen the State's housing deficit and delay the economic multiplier benefits of new housing construction. A dearth of residential construction remains a huge drag on the state's economy, notes the UCLA Anderson Forecast.

The Center for the Continuing Study of the California Economy (CCSCE) describes the devastating effect the decline of the State's housing sector has had on the overall economy.[17] From 2005 to 2009, the decline in annual building permits accounted for much of the 60 percent reduction in construction spending over that span, from nearly $100 billion in 2005 to less than $40 billion in 2009. The report added that California lost nearly 500,000 construction-related jobs during the peak recession between December 2007 and December 2009.

"We will come back big time on employment when housing construction comes back."

Warren Buffet
July 8, 2011, Associated Press

The 2006 report *The Economic Benefits of Housing in California* by Sacramento Regional Research Institute showed that, when the market was still strong, the homebuilding industry generated close to $273 billion in economic output and about 960,000 jobs, accounting for approximately eleven percent of all economic activity in the State.[18]

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[15] CIRB, *California Construction Review*, May 2012
[16] UCLA Anderson Forecast. July 2012. *"Sluggish Economy Continues Despite Improvements in the Housing Market "* http://www.uclaforecast.com/contents/archive/2012/media_62012_1.asp
[17] CSCCE. Stephen Levy. 2010. "*Why is California's Unemployment Rate so High and what does it Mean for the State's Economic Future*". http://www.ccsce.com/PDF/Numbers-Sep2010-Cal-Unemployment-High.pdf
[18] Sacramento Regional Research Institute. 2006. "*The Economic Benefits of Housing in California*". http://www.srri.net/AboutUs/EconBenHousing.pdf

The health of the housing construction industry is critical to the health of California's economy. Estimates for Fiscal Year 2009/10 indicate that a newly built, median-priced home adds more than $375,000 in economic output for the State and creates 2.1 new jobs. [19]

The Center for Strategic Economic Research estimates that, based on 2009 values, new housing construction contributes over $13.8 billion per year to California economy and supports nearly 77,000 jobs statewide on an annual basis.

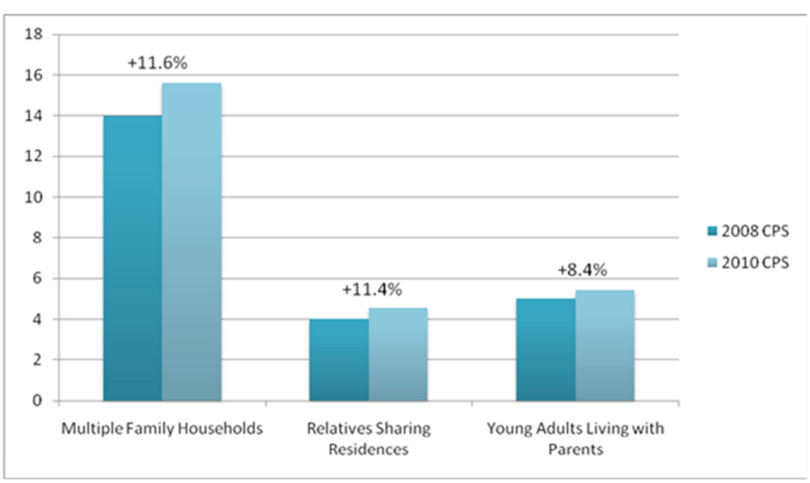
The current inventory of foreclosed units does not offset the need for more housing

California had already fallen behind in its housing need relative to population and employment growth before the Great Recession started. Despite record numbers of foreclosures, the sustained housing deficit is not corrected by the stock of foreclosed homes.

Homes going through the foreclosure process do not automatically become vacant and available for occupancy, because of the time working through the financial and legal systems, and are often held off the market for various reasons. The Joint Center for Housing Studies of Harvard University notes in its *2012 State of the Nation's Housing* that an increased amount of housing held off the market (such as what occurred between 2010-2011) could impact the housing recovery, partially counterbalancing declines in the numbers of vacant homes for rent and for sale.

Even when placed for sale, these units do not increase the overall supply, given the households vacating them must relocate, often to rental units, or with family or friends in shared quarters. Recent analysis found that, between 2008 and 2009, approximately 12 percent of households that moved joined an existing household, a significant increase from 2005, suggesting that more households may be doubling-up and living in overcrowded conditions to better afford housing costs during the current economic downturn.[20]

Evidence of "Doubling Up" in Response to Economic Downturn 2008-2010 (in millions)



Source: U.S. Census Bureau, Current Population Survey (CPS), 2008 and 2010

This is not new for California. In the 1990s, a decline in new construction directly led to dramatic price increases and increased overcrowding. By Census 2000, California had 1.7 million overcrowded households; two-thirds of these were renter households.

Between 2007 and 2010, the US Census Bureau reported an overall increase in the percentage of shared households, from 17 to 18.7 percent in total households, making a correlation between the household sharing and economic strain.

[19] Maya Brennan, Keith Wardrip, June 2010. "*Building California's Future*". http://www.hcd.ca.gov/BuildingCAFuture.pdf
[20] U.S Census Bureau, Newsroom, http://www.census.gov/newsroom/releases/pdf/09-16-10_slides.pdf

The 2010 American Community Survey reported three in four overcrowded households were renter households. More than half of these renters were severely overcrowded. "The recession caused doubling up to save money -- and the story is still unfolding," said Steve Melman, Director of Economic Services for the National Association of Home Builders.

Moreover, the JCHS Harvard 2012 study indicated that foreclosures of single-family and small multifamily properties impact the supply of rentals. In the short term, these units add to the stock of vacant housing held off the market while in the foreclosure process. In the longer term, because many of these foreclosures are in areas where renters are concentrated, they could well accelerate the inventory losses that are already under way. In many urban areas, it could take many years to restore stability to rental housing markets.[21]

The supply of foreclosed vacant homes is substantially reduced, observes Chief Economist of Freddie Mac in a 2012 paper- "The Shadow". In July 2012, Data Quick reported that while 1.45 million of California's roughly 8.7 million houses and condos have been involved in a foreclosure proceeding the past five years, 835,000 went through the whole foreclosure process. The other 615,000 were either sold, or the payments were brought current. The Census Bureau vacancy data showed a continuing decline in overall vacancies in U.S. homes that are for rent and for sale through the second quarter of 2012. The paper indicates US rental vacancy rates declining to the lowest levels since 2002, and for sale vacancy rates decreasing to the lowest since 2006. [22]

"Once the consumers perceive that a floor has formed under housing prices, their re-entry into the market could weekly burn through the lean inventory of unsold new homes and slim down the excess supply of existing homes on the market."

The Joint Center for Housing Studies of Harvard University

State of The Nation's Housing 2011

The Federal Reserve noted in a 2012 whitepaper, "foreclosures can be a costly and inefficient way to resolve the inability of households to meet their mortgage payment obligations because of … costs that do not benefit anyone, including the neglect and deterioration of properties that often sit vacant for months (or even years) and the associated negative effects on neighborhoods." [23]

The good news is that many of these families and children living at homes in doubled up households or in overcrowded conditions may choose to live on their own as soon as their economic condition improves. This could lead to a potential jump in household formation resulting in a boost of housing demand.

[21] The Joint Center for Housing Study Harvard University. April 2008. *"America's Rental Housing: The Key to a Balanced National Policy"* http://www.jchs.harvard.edu/research/publications/americas-rental-housing-key-balanced-national-policy

[22] Frank E. Nothaft, Chief Economist, Freddie Mac. August 2012 U.S. Economic & Housing Market Outlook. August 2012. *"The Shadow".* http://www.freddiemac.com/news/finance/docs/Aug_2012_public_outlook.pdf

[23] Federal Reserve. *"The U.S. Housing Market: Current Conditions and Policy Considerations".* January 2012. Retrieved at:http://www.federalreserve.gov/publications/other-reports/files/housing-white-paper-20120104.pdf

There is a mismatch between the existing housing stock and the demand for housing by type and location

Much of the existing housing stock does not meet current consumer demands. A 2012 analysis published by the Joint Center for Housing Study of Harvard University looking into the drivers of preferences for renting or ownership during 2007-2009, suggests that, despite the housing market downturn, the appeal of homeownership remains strong. Per Fannie Mae's 2011 National Housing Survey, 85 percent prefer owning because financially it makes more sense than renting.[24]

> ***"We continue to see a strong demand for housing, but the California market is being hindered by a lack of inventory and multiple offers on what little inventory that is available"***
>
> ***LeFrancis Arnold, CAR President***
>
> ***August 2012***

Many young adults hard hit by the recession enter a weak job market and may choose renting closer to job opportunities, in a more urban living setting than their predecessors, demanding smaller homes close to jobs, services and transit. Some older Californians may also need to downsize to more affordable units close to amenities or services. While many are unable to sell and move, the ones that do will downsize.[25] The average size of new homes between 2007 and 2010 declined to 2004 levels and it is projected to decline to 1995 levels.

Homeowners unable to sell or refinance due to negative equity or depressed prices may defer maintenance and occupy units in need of repair. Also, many of the smaller homes and apartments which account for a higher share of affordable units in the existing stock are older and often substandard and may be lost to demolition. Single family homes that are foreclosed, vacant or abandoned are often in need of rehabilitation. These conditions widen the gap between the supply and demand for affordable rental units.

Existing housing stock, including the substantial subset of vacant foreclosed units for sale in the suburbs, will not meet the need or the demand for more infill housing accessible to jobs and transit in more central locations, necessary to reduce the costs of energy, transportation and greenhouse gas emissions. Nor does the existing housing stock meet the need for a greater supply of a mix of housing types including "greener" development, smaller homes, or mixed-use housing.

A 2011 study by economists Denk, Dietz and Crowe maintains that high vacancies in some areas in the current market are not a sign of overbuilding, but rather an indication of significant pent-up demand related to economic conditions. The study implies that recovery in the housing market will come more quickly as the economy recovers and pent-up demand becomes realized demand, absorbing vacant units in the existing stock and adding pressure for the construction of new units.[26]

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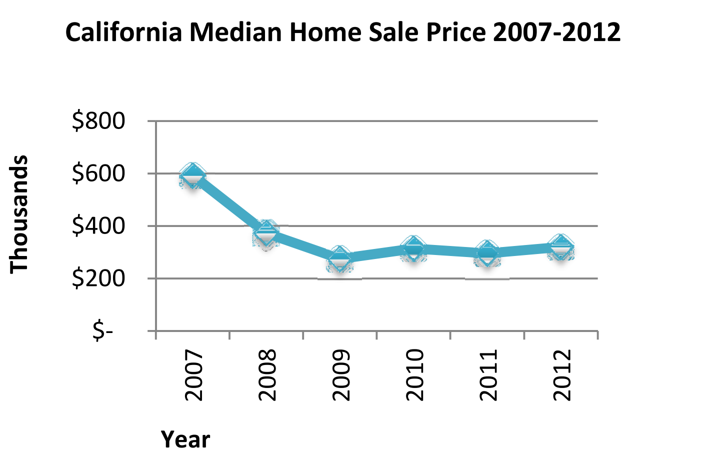
[24] Rachel Bogardus Drew, Christopher Herbert. "Post-Recession Drivers of Preferences for Homeownership". August 2012. http://www.jchs.harvard.edu/research/publications/post-recession-drivers-preferences-homeownership
[25] The Demand Institute. May 2012. "*The Shifting Nature of U.S. Housing Demand*". *p31*
[26] Robert Denk, Robert Dietz, Ph.D. and David Crowe, Ph.D Economics & Housing Policy , "Pent-up Housing Demand: The Household Formation That Didn't Happen-Yet", Special Studies, February 2, 2011

III. Housing Affordability

Homeownership: The State's chronic housing affordability gaps have not been eliminated despite lower housing prices

Affordability represents the relationship between housing prices and incomes; in order for housing to become more affordable, its prices need to fall by more than the decline in income. By this standard, despite the fall in housing prices, USC Professor Myers' "California Roller Coaster-Income and Housing in Boom and Bust, 1990-2010" study found housing did not become more affordable, as prices did not decline enough to compensate for the loss in income.[27]

The Bureau of Labor Statistics reported the State's unemployment rate doubled from 2008 to March 2011, reaching 12 percent. Preliminary data for 2012 shows a 10.7 percent unemployment rate.[28] Between 2008 and 2009, California's homeowner households declined by an estimated 130,000. In 2000, 56.9% of households were homeowners, spiking upward to 58.4% in 2006. With the collapse of the financial market, the homeownership rate plunged 2.5 percent to 55.9 percent in 2010, and to 55.3 percent in 2011, as recessionary conditions have swelled the ranks of renters, overcrowded housing units, homeless, and families struggling to meet food, housing, and transportation needs.



Source: California Association of Realtors. "Trends". 2011. 2012

Median home prices statewide peaked at $534,300 in March 2006, and declined steeply, reaching $337,500 in 2010. By June 2011 the median sales price had decreased another 5.9 percent when compared to June 2010. Six months later it decreased further at 6.2 percent over the previous year.[29]

By June 2012, home prices increased moderately, reaching $320,540 for a single family detached home, an eight percent increase from June 2011, yet still below the 2010 level. Although the trend of rising home prices is noted in most of the State's housing markets, the variability between regional median prices is significant: while in the Inland Empire area the median price for single-family homes as of July 2012 was $191,130, the Los Angeles Metropolitan Area and San Francisco Bay Area reached significantly higher median sale prices, reaching $315,200 and $579,540, respectively.[30]

While in some markets, homeownership has become more affordable, especially for first-time homebuyers, housing remains out of reach for many lower-income families and workers, due to unemployment or underemployment, lack of available financing and tightened underwriting standards.

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[27] Idem., Dowell Myers, Ray Calnan, Anna Jacobsen and Josh Wheeler, p.8
[28] U.S. Bureau of Labor Statistics, *"California at A Glance"*, August 2012. http://www.bls.gov/eag/eag.ca.htm#eag_ca.f.P
[29] California Association of Realtor's, *"Trends"*. Vol. 32. : No. 2. March 2011, No.7, July 2011, No.1 January 2012
[30] California Association of Realtors. August 2012. *"July home sales and price report"*. http://www.car.org

The steep decline in prices over the years also left many homeowners “underwater” in their mortgage loans, and trapped in homes worth less than the mortgage balance, unable to sell. The Public Policy Institute of California reported CoreLogic estimates 30 percent of mortgaged residential properties in the state were “underwater” in the second quarter of 2011, the fifth highest percentage in the nation after Nevada, Arizona, Florida, and Michigan.[31]

In addition, California had the highest share of housing cost burden in the nation, at 51.2 percent[32], and of working households with a severe housing cost burden at 34 percent of total households in 2010.[33] In actual numbers, more owners are cost burdened than renters because the homeownership rate for older adults is so high, but in general, renters are more likely than owners to spend a very high portion of their income on housing. More than 8.5 million households headed by an adult age 65+ spend more than 30 percent of their income on housing costs and 4.6 millions of this spend *more than half their income* on housing.

Others, such as former homeowners, young adults or new immigrants will have no choice but to remain in the rental market until finances improve. Many households, as the Center for Public Policy suggests, may prefer renting for reasons as varied as concerns about home price volatility, uncertainty about affording the costs of major repairs, and mobility or a desire to have greater access to job opportunities elsewhere.[34]

“It’s hard to generalize the state of California’s housing market because the markets are so diverse and are performing so differently…REO-dominated areas such as those in the Inland Empire and Central Valley are experiencing sales constraints due to an extreme shortage of available homes. On the other hand, a robust economy in the San Francisco Bay area and a relatively larger inventory at higher price levels is helping to fuel sales and prices.”

C.A.R. President LeFrancis Arnold

July 2012

Rental housing: California has a large unmet need for rental housing affordable to lower-income households

During the past decade, California’s rental market did not follow the same trajectory of boom and bust as the homeownership market. While housing prices declined from 2006 to 2011, rents increased throughout the state by an average of ten percent, tightening the rental housing market.[35] As the 2010 Census revealed, rental vacancy rates in California (6.3 percent) were well below those in the rest of the nation (9.2 percent) in 2010. This greatly impacted California’s households that have been hit hard by the Great Recession. Income has declined for all the income categories, with lower income households seeing the most substantial losses, the gap between upper- and lower-income households widening, and the middle-income range shrinking.

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[31] Public Policy Institute of California, *“California’s Housing: Planning for a Better Future”.* February 2012. http://www.ppic.org/content/pubs/report/R_212HJ3R.pdf

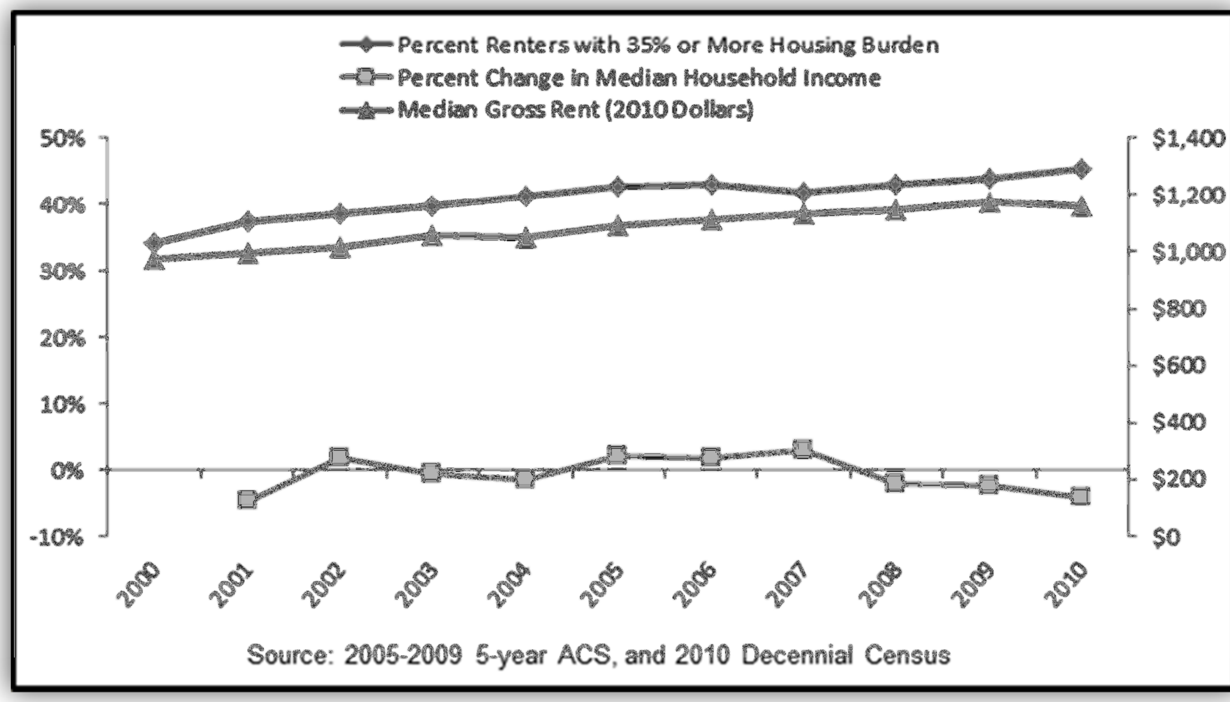
[32] Public Policy Iinsitute of California. 2012. *“The Economy Key Statistics – Housing Market Indicators”* *http://www.ppic.org/main/keystat.asp?i=1250*

[33] Housing Landscape 2012: Center for Housing NLIHC

[34] Center for Housing Policy “Paycheck to Paycheck 2011: Is housing affordable for Americans getting back to work?”, Maya Brennan and Laura Williams , July 2011

[35] Public Policy Institute of California, Hans Johnson, April 2012, “*California’s Housing Market*”, http://www.ppic.org/main/publication_show.asp?i=1009

This is a significant trend for the rental market, as lower income households comprise the majority of renter households. According to 2010 American Community Survey, out of 5.1 million renters in California, 60 percent are lower-income households, while one in four renter households is in the extremely low income category (ELI). And almost three in four lower income renters are housing-cost burdened.[36]



The "*Paycheck to Paycheck 2011*" report by the Center for Housing Policy indicated that ten of the twenty least affordable rental markets in the United States are in California. One in two renters in California pay in excess of 30 percent of their income, while one in four renters pay more than half of their income toward rent.

Three in four ELI renters spend more than 50 percent of their income on housing. The 2012 update of the prior report found that in high-priced communities, teachers, police officers, nurses, and accountants do not earn enough to afford typical rents or home prices, and that even in moderately-priced communities, people who work a full-time job pay an excessive portion of their income for housing. Half of the metropolitan areas ranked as least affordable rental markets nationwide are from California, while only three, or less than five percent of the areas with better affordability than that of the nation are within the State.[37]

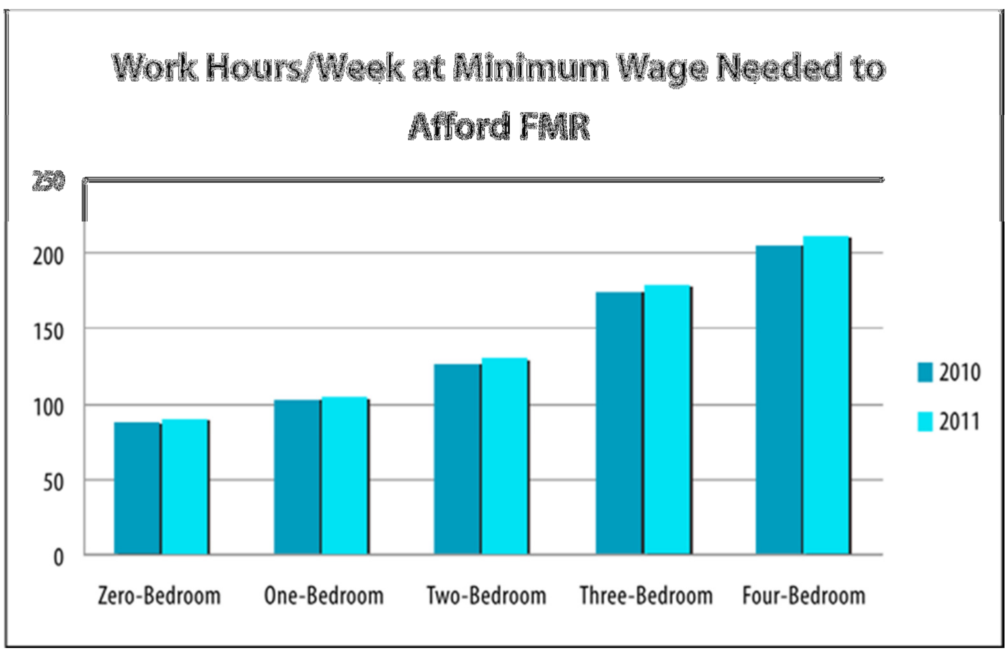
The foreclosure crisis exacerbated renter housing needs; an estimated 38 percent of homes in foreclosure were rentals, resulting in more than 1 million California renters being directly affected (175,000 in 2011 alone), many of which were evicted and moved in unstable, tenuous living situations after eviction.[38] In 2011, HUD reported to Congress that housing needs of low-income renter households with high housing costs or occupying severely substandard housing increased more than

[36] Paying in excess of 30 percent of income for rent and utilities. Severely housing cost burdened households are households paying in excess of 50 percent of their income toward housing cost.
[37] National Housing Conference (NHC), *"Paycheck to Paycheck"*, July 2012, http://www.nhc.org/chp/p2p/
[38] Tenants Together. July 2012. *"California Renters in the Foreclosure Crisis"* , Fourth Annual Report,. http://tenantstogether.org/downloads/4th%20Annual%20Report.pdf

20 percent from 2007 to 2009. Unfortunately, only a quarter of eligible households nationally actually receive tenant-based rental assistance, leaving a large proportion of renter households paying too much for housing, doubling up, or living in substandard conditions.

Per the 2011 *California Federal Rent Assistance Facts* by the Center on Budget and Policy Priorities, out of 3.1 million lower-income renter households in California, only 466,244 are federally assisted and can afford modest housing at an affordable housing cost. Approximately 60 percent of the assisted households are headed by people who are elderly or disabled; approximately 30 percent are families with children. There are another 1.4 million low-income renter households that pay more than half of their monthly cash income for housing costs. On average, these households have incomes of $1,291 and pay housing costs of $1,143, leaving only $148 to pay for other necessities. About 31 percent of these severely cost-burdened renters are elderly or people with disabilities, while 38 percent are families with children.

According to the National Low Income Housing Coalition, affordability of rental housing has worsened in California since 2007. In 2007, a minimum wage renter had to work 120 hours per week to afford a two-bedroom apartment. In 2010, the number of hours increased to 128, and reached 131 in 2011. In 2012, a household must include 3.3 full-time minimum wage jobs to afford a two-bedroom rental.[39]



Source: National Low Income Housing Coalition: http://www.nlihc.org/oor

Also contributing to the tightening of the rental market is the increased number of middle-income households choosing or finding it necessary to rent, as homeownership rates decline, further limiting housing options for low income renters. A shift in tenure due to foreclosures tightened the rental markets further driving increased rents. As rental housing demand continued to rise and the vacancy rate dipped to the lowest level since 2001, rental housing costs increased impacting the lower income households.[40]

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[39] The National Low Income Housing Coalition (NLIHC), *"Out of Reach",* July 2012 *http://www.nlihc.org/oor*
[40] National Low-Income Housing Coalition. *2012 Out of Reach*. 2012.: http://nlihc.org/oor/2012

Not all the units that are affordable are available for rent, as many of those units are occupied by higher income renters, are in poor, unsafe condition, or are located too far from jobs and public transportation. For example, the National Center for Housing finds that for every 100 very low income renter households there were only 87 affordable units in 2010. For every 100 extremely low income renters (ELI), there were only 56 units affordable.

> *"The rising incidence of housing cost burdens among renters makes evident the urgent need for expanding the supply of affordable housing."*
> *Out of Reach 2012*

Experience since 2010 hasn't shown much improvement. The National Low Income Housing Coalition shows in its *2012 Out of Reach* report that the average ELI household will earn roughly over $20,000 and can only afford $505 for rent. Yet, a one-bedroom for-market-rent is $797, one-and-a-half times more expensive; two-bedroom housing is almost twice as expensive as what an ELI household can afford. As a result, three in four ELI renter households spend more than half of their income on housing costs. [41]

The Joint Center for Housing Studies of Harvard University recently emphasized the renewed importance of an adequate supply of affordable rental housing, as today's economic and demographic conditions boost rental demand. It describes the diverse rental needs for what is a disproportionately large share of single–person, young and minority households concentrated at the bottom half of the income distribution, indicating that nearly three-quarter of renters have incomes below median income for all households.[42] The pressure is likely to continue in lower-rent market segments. This is not a signal of added supply but rather that more of the affordable stock has become uninhabitable.

Preservation of affordable housing is critical in this economy

Thousands of units of privately-owned, publicly-assisted multifamily rental housing are at risk of conversion to market rate rents. These affordable units are often funded through multiple programs, including federal, redevelopment, State and local programs. The potential loss of these units directly impacts the State's affordable housing stock. Amid rapidly rising rental costs and the tightening of available resources at the federal, State and local levels, preserving California's existing affordable housing is critical.

California Housing Partnership Corporation (CHPC), a private nonprofit organization dedicated to helping government and nonprofit housing agencies preserve and expand the supply of affordable housing in California, estimates 68,000 of the federally subsidized affordable apartments in California are at-risk of conversion to market rate in the next five years, with an additional 74,000 becoming at-risk in the following 15 years.

[41] The National Low Income Housing Coalition (NLIHC), "Out of Reach", June 2010, June 2011 and 2012 http://www.nlihc.org/oor

[42] Joint Center for Housing Studies of Harvard University, "America's Rental Housing : Meeting Challenges, Building on Opportunities, 2011", http://www.jchs.harvard.edu/publications/rental/rh11_americas_rental_housing/AmericasRentalHousing-2011.pdf

Tens of thousands of project-based Section 8 contracts in California will expire over the next decade without any assurance of renewal by the private landlords who own them, potentially ending the subsidies that ensure affordable housing for thousands of low-income families in the State. In the next five years alone, 60,617 units in 897 properties are at-risk of conversion to market rate. Almost half of these units will reach their expiration dates in 2013.

Reconnecting America, a non-profit organization that conducted a study in 2012 on efforts needed to protect assisted affordable housing projects in Los Angeles Area, found that preservation of the affordable housing stock is important for a variety of reasons including:[43]

- The affordable housing stock is at risk more so than ever before. In the Los Angeles area, nearly 15,000 income-restricted units have covenants, rental assistance contracts, mortgages, or other time-limited affordability requirements that will expire or are at risk of being terminated between 2012 and 2017.
- As transit catalyzes reinvestment in transit-rich neighborhoods, lower income residents and workers risk displacement to areas with fewer transportation and employment choices.
- Economic competitiveness relies on offering housing for workers of all incomes. For example, a majority of the jobs of the fastest growing sectors such as health services will be filled by low- and moderate-income workers, while many workforce development institutions are located along the transit system connecting low-income workers to better job opportunities through training and education.

Collaboration with key partners on preservation efforts can prevent the potential loss of a significant share of the affordable housing stock, and create opportunities to identify and acquire transit-oriented properties for long-term preservation or development.

Why preserve existing affordable rental housing?

• New construction alone cannot produce enough affordable housing to meet demand in most markets in California.

•On average it serves lower income households than new construction.

• It is less costly and takes less time than new construction.

California Housing Partnership Corporation website:

http://www.chpc.net/preservation/newsletter.html

[43] Abigail Thorne-Lyman and Jeffrey Wood. May 2012. *"Preservation in Transit-Oriented Districts: A Study on the Need, Priorities, and Tools in Protecting Assisted and Unassisted Housing in the City of Los Angeles".* http://www.reconnectingamerica.org/resource-center/books-and-reports/2012/preservation-in-transit-oriented-districts-a-study-on-the-need-priorities-and-tools-in-protecting-assisted-and-unassisted-housing-in-the-city-of-los-angeles/

Conclusion

Aggressive actions to increase the supply and affordability of housing, support the residential construction industry, and preserve existing affordable housing stock are critical to supporting California's economic competitiveness and improving the quality of life for its residents. This is fundamental for California to maintain its leadership role in addressing climate change and environmental quality while adequately housing workers and families.

"Improvements in affordability require both increasing renter incomes and moderating housing costs. But with persistently high unemployment, the prospects for renter income gains are dim and rising demand for rental housing may well put added pressure on rents. Moreover, global energy demand is almost certain to grow, further limiting the ability of the poorest renters to afford housing."

Joint Center for Housing Studies of Harvard University, "America's Rental Housing: Meeting Challenges, Building on Opportunities, 2011"

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This paper can be retrieved at: http://www.hcd.ca.gov/hpd For more information or questions, please contact Anda Draghici, Senior Housing Policy Specialist, Division of Housing Policy Development, at (916) 445-4728.

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