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CENTER FOR  
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# California Homeownership in 2030 and Beyond:

## DEMOGRAPHIC CHANGE AND THE “LOST GENERATIONS” OF HOMEOWNERS

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**Lowell R. Ricketts**, LEAD ANALYST, CENTER FOR HOUSEHOLD FINANCIAL STABILITY

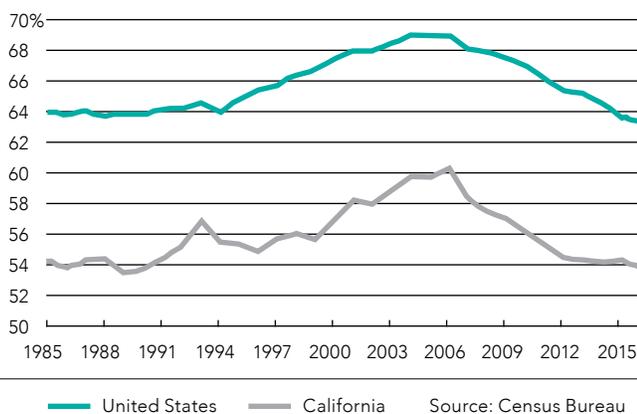
### KEY TAKEAWAYS

- The homeownership rate in California has trailed the rest of the U.S. by about 10 percentage points for decades.
- California’s unique demographic mix and poor housing affordability are important explanations for why the California homeownership rate is below the national average.
- Detailed demographic projections suggest the “California homeownership gap” is likely to persist until at least 2030.
- Despite a stable homeownership gap overall, changing demographics and the long-lasting impacts of the recent housing crisis are powerful crosscurrents operating below the surface.

### Case Study Abstract

*The homeownership rate in California has trailed the rest of the U.S. by about 10 percentage points for decades. Detailed demographic projections suggest the “California homeownership gap” is likely to remain stable until at least 2030, even as homeownership rates drift down in California and nationwide. The changing racial and ethnic mix of the California population will reduce the gap, as will the entry of young families into homeownership that were not affected by the housing crisis. A factor working in the opposite direction is the eventual replacement of older California homeowners with high homeownership rates by current baby boomers and members of Generations X and Y, who suffered large declines in homeownership during the crisis. To mitigate the long-run decline in California homeownership, families hit hard by the housing crisis require balance sheet repair. Housing supply-side reforms that make housing more affordable also could help.*

Figure 1  
**HOMEOWNERSHIP RATES U.S. AND CALIFORNIA**



## Case Presentation

Despite significant variation over time, California’s homeownership rate – the share of households that own their homes – has remained about 10 percentage points below the national rate for at least three decades (see Figure 1). We believe the “California homeownership gap” will remain at about that level until at least 2030, even as homeownership rates drift down across the country. However, this apparent stability belies important shifts taking place below the surface that could eventually widen the gap.

middle-aged families. Second, artificial barriers to homeownership could be addressed through supply-side reforms that make housing more affordable.

### THE RECEDING TIDE: GENERATIONAL TRENDS IN CALIFORNIA HOMEOWNERSHIP

California’s seniors – roughly speaking, people born in 1950 or before – have attained homeownership rates higher than any previous or subsequent generations. Californians born after 1950, on the other hand, are less likely to be homeowners than

Table 1 **GENERATIONS IN THE U.S. AND CALIFORNIA POPULATIONS**

GENERATION	BIRTH YEARS	MEMBERS IN THE US IN 2015 (millions)	MEMBERS IN CALIFORNIA IN 2015 (millions)
Greatest	1900-25	3.0	0.3
Silent	1926-45	31.2	3.4
Baby boom	1946-64	76.8	8.7
Generation X	1965-80	65.6	8.3
Generation Y (Millennials)	1981-2000	87.9	11.3
Generation Z	2001-15	56.8	7.1

Source: Census Bureau

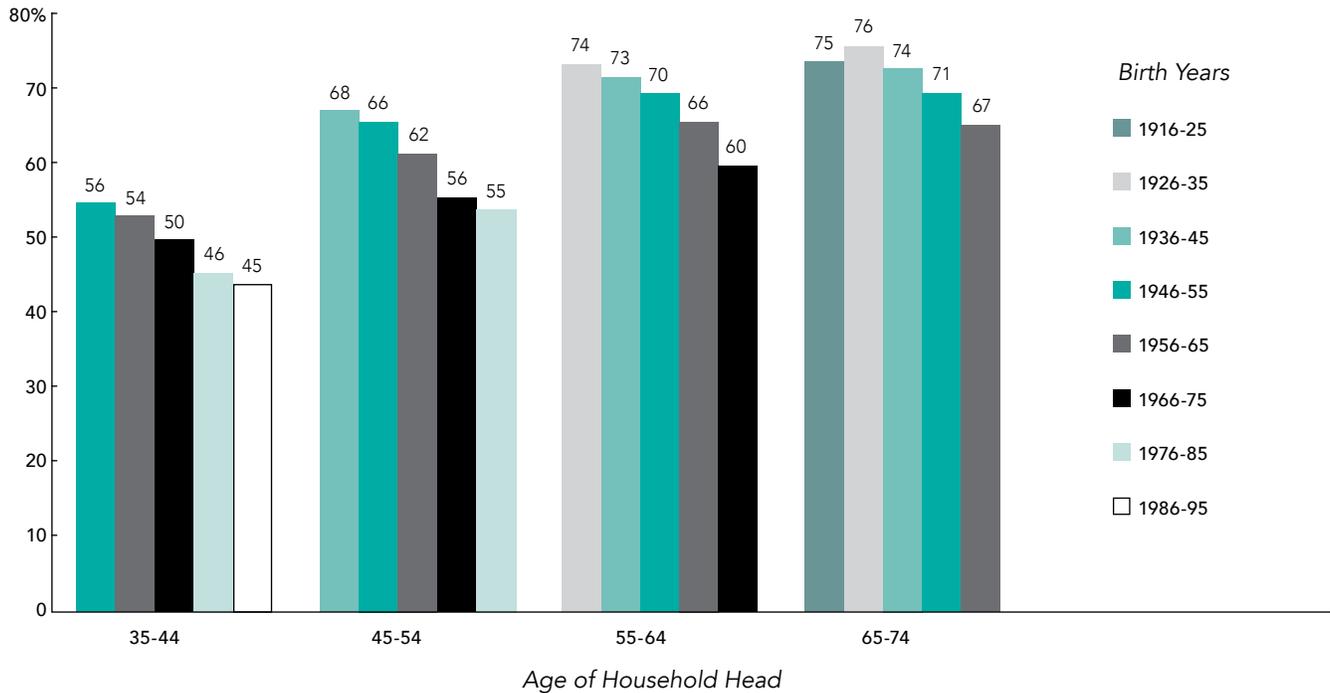
Perhaps surprisingly, California’s changing demographics actually will reduce the state’s homeownership gap vs. the rest of the country between now and 2030. This is because, in important respects, the rest of the country is expected to change even more rapidly than California. On the other hand, several “lost generations” of homeowners will drag down the California homeownership rate as older generations with very high homeownership rates pass on. While young families across the nation bore the brunt of the housing crash, young Californians were especially hit hard.

How could the long-term trend toward declining homeownership, both in California and elsewhere, be mitigated? First, efforts should be directed toward the repair of damaged household balance sheets, especially among young and

their elders at comparable life stages. Moreover, our projections suggest that several “lost generations” of Californians – including late baby boomers and members of Generations X and Y (the latter which is also known as “millennials”) – are on track to reach homeownership rates far below those of the so-called Greatest and Silent Generations who came before them (See Table 1 for information about the status of generations).

Figure 2 shows actual and projected homeownership rates for groups of California households headed by someone born between 1916 and 1995 as they pass through middle age. Clearly, homeownership rates have been falling among successive generations as they reached each age range.<sup>1</sup> For example, 56 percent of California households headed by someone born between 1946 and 1955 – early baby boomers –

**Figure 2 CALIFORNIA HOMEOWNERSHIP RATES BY AGE AND BIRTH YEAR:  
ACTUAL, 1990-2010 AND PROJECTED, 2020-30**



Source: Census Bureau/IPUMS, Urban Institute, our calculations.

were homeowners when they were between the ages of 35 and 44.<sup>2</sup> For households headed by late baby boomers born between 1956 and 1965, the homeownership rate was only 54 percent. Finally, for Generation X members born between 1966 and 1975, the homeownership rate fell to 50 percent. Our model predicts that the homeownership rate among households in this age group will fall to 46 percent among households headed by someone born between 1976 and 1985 (spanning Generations X and Y); and to 45 percent among households headed by someone born between 1986 and 1995 (Generation Y).

The pattern of declining homeownership across generations is qualitatively similar in each of the remaining age ranges depicted in Figure 2. For the age range of 45 to 54 years, the homeownership rate was 68 percent among households born between 1936 and 1945;<sup>3</sup> but it is projected to be only 55 percent for households headed by someone born during the timeframe of 1976-1985. For the age range of 55-64 years, the homeownership rate was 74 percent among households born between 1926 and 1935.<sup>4</sup> The Center for Household Financial Stability at the Federal Reserve Bank predicts it will be only 60 percent when households headed by someone born between 1966 and 1975 reach

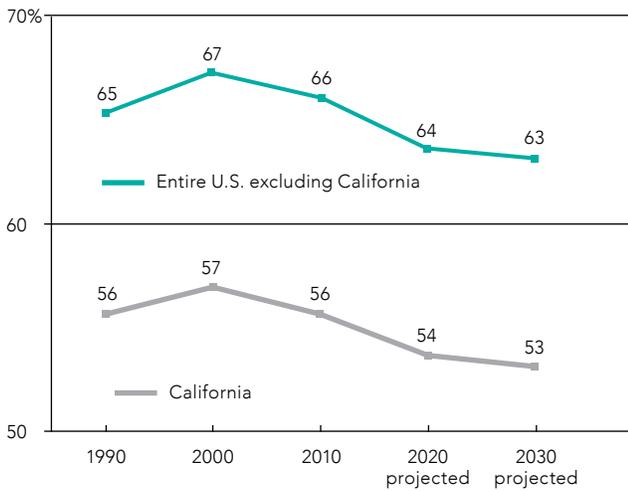
<sup>1</sup>This is true also in the rest of the United States but to a somewhat lesser extent.

<sup>2</sup>This data point is derived from the 1990 census. At the time of the 2000 census, this cohort was in the 45-54 age range, as shown in the second set of bars in the chart. At the time of the 2010 census, they were in the 55-64 age range, shown in the third set of bars. We use Census Bureau projections and a model designed by the Urban Institute (see Goodman et al. 2015) to project this cohort's homeownership rates in 2020 (fourth set of bars) and 2030 (not shown), when they will be in the age ranges 65-74 and 75-84, respectively.

<sup>3</sup>This data point is from the 1990 census.

<sup>4</sup>This data point is from the 1990 census.

**Figure 3 HOMEOWNERSHIP RATES:  
ACTUAL AND PROJECTED**



Source: Census Bureau/IPUMS, Urban Institute, our calculations.

that age range. The final two sets of bars in Figure 2 hint that households headed by someone born between 1926 and 1935 experienced the highest homeownership rates of any birth cohort at nearly every age.<sup>5</sup>

### HOMEOWNERSHIP RATES LIKELY TO DECLINE, BUT THE CALIFORNIA GAP SHOULD REMAIN UNCHANGED UNTIL 2030

Replacement of older cohorts, who have relatively high homeownership rates by younger cohorts with lower homeownership rates, is likely to result in declining overall homeownership rates both in California and nationwide, as Figure 3 shows. We expect California’s gap of 10 percentage points relative to the U.S. to remain unchanged at least until 2030, despite a somewhat more precipitous generational homeownership decline among aging Californian baby boomers and members of Generations X and Y than their counterparts elsewhere.<sup>6</sup> What other forces are at work?

For example, comparing only households headed by someone in the 55-64 age range, the generational decline in homeownership rates will be about 14 percentage points in California between 1990 and 2030, but only about 10 percentage points in the rest of the United States. First, while the share of households headed by whites is expected to decline in California between 2010 and 2030, the rate of decline will be slower than in the rest of the nation. This is important because whites are the largest group in both the California and U.S. populations and their homeownership rates are substantially higher than among blacks, Hispanics and other groups, including Asians.

By 2030, it is projected that the share of white households in California’s population will fall by about 5 percent, compared with a national decline of 8 percent. This alone will put greater downward pressure on the homeownership rate outside California, closing some of the state’s homeownership gap.

A second important factor is our assumption that future young Californians will have homeownership rates closer to their counterparts elsewhere than is true of recent cohorts, who were hit hard by the housing crash – especially in California. For example, we expect the California homeownership gap among households in the 25-34 age range to decline 2.5 percentage points between 2010 and 2030, although the absolute level of the gap will remain sizable – about 12.4 percentage points. Among households aged 35-44, we expect the gap to decline by 1.8 percentage points, leaving it at 12.5 percentage points in 2030.

### BEYOND 2030: MINDING THE GAP

Our projections suggest that several powerful forces are likely to offset each other to leave the California homeownership gap relative to the rest of the nation relatively stable between now and 2030. However, the long-run gap could widen. This is because an important part of the story is a partial

<sup>5</sup>This is true both in California and nationwide.

<sup>6</sup>For example, comparing only households headed by someone in the 55-64 age range, the generational decline in homeownership rates will be about 14 percentage points in California between 1990 and 2030, but only about 10 percentage points in the rest of the United States.

recovery in the homeownership rates of young and middle-aged Californians, compared with their counterparts elsewhere. But this effect will fade eventually as the most affected generations – late baby boomers and members of Generation X and Y – pass on.

How could the California homeownership gap be reduced? Financially weaker families in California – especially among the generations most affected by the crash – need to shore up their balance sheets or receive help in doing so. Second, poor housing affordability and a history of boom-bust cycles in California housing markets also weigh heavily. Reducing supply-side restrictions that artificially raise the cost and volatility of housing could moderate, if not eliminate, the California homeownership gap. ■

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# Can Americans Rebuild Their Assets if Asset-Building is No Longer a Political Priority?

By **Doug Ryan**, DIRECTOR OF AFFORDABLE HOMEOWNERSHIP,  
CORPORATION FOR ENTERPRISE DEVELOPMENT (CFED)

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## KEY TAKEAWAYS

- Homeownership in the United States remains at – or near – historic lows across the country and the state of California.
- African-American and Latino homeownership rates hover well below peaks, with rates for African-Americans at levels unseen since the 1960s.
- While improvements in regulations have limited or eliminated many of the predatory loan products that caused the financial crisis, tools remain underutilized to spur credit access.
- Federal programs that advance homeownership leverage private capital, create jobs, and expand tax bases; consequently, they should be embraced.

## Case Study Abstract

*Although the U.S. economy has recovered from the depths of the financial crisis, for many Americans, the homeownership market, which drove the crisis, has not. Homeownership rates across demographics and regions are at historic lows, and mortgage credit remains constrained for many potential buyers. California buyers, in particular, face a greater strain, as the state's homeownership rate has long trended below national rates.*

*Access to credit is just one challenge. Raising down payments, accessing good counseling, and other components of first-time home-buying are also under threat by poor budget proposals and false narratives about the housing crisis. Limited starter and trade-up homes also undercut the market.*

*This case study proposes some near- and mid-term steps the federal government can take to advance homeownership. While the Trump administration cannot solve the inventory problem on its own, it can revisit early decisions that will undercut access to the American Dream in California and beyond.*

## Case Presentation

In the 2016 election, presidential candidates did not spend much time discussing housing or homeownership. It came up just once in the debates in September, when former Secretary of State Hillary Clinton suggested that the Republican nominee Donald Trump had “rooted for the housing crisis.” While Clinton had detailed housing policies on her campaign website, Trump minimally addressed the issue. More importantly, the media – from debate moderators to editorial page interviewers to radio hosts – barely raised the issue of homeownership. That’s remarkably short shrift for a sector that accounts for nearly an eighth of the American economy and drove the worst financial crisis since the 1930s.

Housing and homeownership policy have long lived under the radar of American politics. That is not going to change anytime soon, but there are real discussions underway in Washington that will impact the housing markets in California and beyond and can have long-standing influence on the asset- and wealth-building potential of current and future home buyers for years to come.

Let us start with where we are today. The nation and California’s homeownership rates are near historic lows.<sup>1</sup> The rate in California is among the lowest in the nation, at about 54 percent. Not surprisingly, specific cities and regions are also seeing declines. Los Angeles, according to one recent report, has the lowest homeownership rate among major

metropolitan areas.<sup>2</sup> Also, the drop seen in ownership – and wealth – is uneven.

The state of California reports that African-American homeownership averaged about 35 percent between 2010 and 2014<sup>3</sup>, well below the national rate (which is down to 41 percent, a level unseen since the enactment of the Fair Housing Act in 1968). The impact on Latino home buyers has been similar. The wealth of these communities has been decimated.

All of these factors underscore the challenges before homeownership advocates and policymakers. These challenges are even more stark when considering that although mortgage rates are at historic lows, they are trending higher, which will continue in the near term. Home prices also will rise nationwide and in most markets, too. In the last year, Zillow has reported that home values rose nearly seven percent. While price escalation is well known in markets, such as in the Bay Area and San Diego, smaller, less expensive markets, such as Stockton and Visalia, are also seeing significant home price appreciation.<sup>4</sup>

Finally, the credit box is showing only recent signs of loosening. According to the Urban Institute,<sup>5</sup> the median credit score for mortgage borrowers in March was 732. Notably, about 45 percent of the U.S. population has a score below 700.<sup>6</sup> To their credit, Fannie Mae and Freddie Mac, through the support of their regulator, the Federal Housing Finance Agency, have taken measures to expand access to credit in recent months.<sup>7</sup>

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<sup>1</sup> Federal Reserve Bank of St. Louis. *Economic Data*. Available online at <https://fred.stlouisfed.org/series/USHOWN> and <https://fred.stlouisfed.org/graph/?g=7uJB>

<sup>2</sup> Woo, Andrew and Dylan Grosz. *Homeowners and renters – a widening gap*. Apartment List. August 11, 2016. Available at <https://www.apartmentlist.com/rentonomics/widening-gap-between-owners-renters>

<sup>3</sup> California Department of Housing and Community Development (2017). *California’s Housing Future: Challenges and Opportunities*. Available online at <http://www.hcd.ca.gov/policy-research/plans-reports/docs/California’s-Housing-Future-Full-Public-Draft.pdf>

<sup>4</sup> Zillow. *Local Market Overviews*. February 2017. Available at <https://www.zillow.com/research/local-market-reports/#all-reports>

<sup>5</sup> Goodman, Laurie, Alanna McCargo, Ellen Seidman, Jim Parrott, Sheryl Pardo, Jun ZhuBing, Bai Karan Kaul, Maia Woluchem, Bhargavi Ganesh and Alison Rincon. *Housing Finance at a Glance: A Monthly Chartbook*, March 21, 2017. Available at [http://www.urban.org/research/publication/housing-finance-glance-monthly-chartbook-march-2017/view/full\\_report](http://www.urban.org/research/publication/housing-finance-glance-monthly-chartbook-march-2017/view/full_report)

<sup>6</sup> FICO Blog. *US Credit Quality Continues To Climb – But Will It Level Off?* August 18, 2015. Available at <http://www.fico.com/en/blogs/risk-compliance/us-credit-quality-continues-climb-will-level/>

<sup>7</sup> Goodman, Laurie. *Quantifying the Tightness of Mortgage Credit and Assessing Policy Actions*. March 9, 2017. Available at <http://www.urban.org/research/publication/quantifying-tightness-mortgage-credit-and-assessing-policy-actions>

The price, rate, and credit availability trends suggest that time is running out before the nation loses a generation of homeowners, and with it, a loss of wealth-building for generations.

Here's why: Many Americans, especially white Americans, benefit from intergenerational transfers of wealth, most notably for a first-time home purchase. White families are three times as likely as black families to use family assistance to fund down payments.<sup>8</sup> In turn, this gives the typical white homeowner an eight to 10-year head start to build equity, along with more time to recover from market downturns.<sup>9</sup>

So now what?

In normal times, we would resort to good public policy to drive good outcomes. In our current environment, it's hard to say what lies ahead. Good ideas, and initial first steps, are out there to start the conversation.

Unfortunately, the Trump Administration erred when it reversed a new Obama policy that would have reduced the cost of mortgage insurance from the Federal Housing Administration (FHA), the arm of the U.S. Department of Housing and Urban Development (HUD) that insures mortgages to borrowers generally deemed too risky for the conventional market. If left in place, the reduction would have helped about 250,000 new home buyers over three years, saving \$500 per borrower each year.<sup>10</sup> FHA is healthy enough to support this change, and critics of the Obama proposal are off the mark. Reinstating this reduction would be a good first step by HUD Secretary Ben Carson to show support for the American Dream. This would also offer these new homeowners the jump-start they need to build wealth.

Another step the administration can take, which it could do with assistance from Congress and its constituents, is to rethink the so-called skinny budget's impact on housing. The budget will be devastating to low- and moderate-income communities, and will not be adopted as-is. However, it sends a signal about the administration's priorities. In the last 12-15 years, California, like all states, has seen drastic reductions in key federal programs such as the Community Development Block Grant and HOME. The January 2017 draft of *California's Housing Future: Challenges and Opportunities* notes how these and other programs have funded down payment assistance, home repair, and other vital initiatives to facilitate and sustain wealth building through homeownership.<sup>11</sup> These federal dollars leverage private and other sources, as well as bring homeownership, revenue, and jobs to local communities. Furthermore, gutting them makes little practical sense.

Eliminating the Community Development Financial Institutions (CDFI) Fund and the Neighborhood Reinvestment Corporation is also counterproductive. The CDFI Fund supports local and regional nonprofit lenders, which often lend in areas abandoned or underserved by private capital. In 2016, the CDFI Fund supplied grants to 32 California organizations, many of which provide mortgages and other housing services to qualified borrowers. Eliminating the fund will simply eliminate credit from already credit-hungry – and credit-worthy – borrowers.

The Neighborhood Reinvestment Corporation includes NeighborWorks America, a network of 240 nonprofit housing and community organizations that counsel, lend to, and support families, leading to tangible outcomes. These organizations, including 21 in California, have measurable success in preparing families to purchase homes and in

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<sup>8</sup> Shapiro, Thomas M. *The Hidden Cost of Being African American: How Wealth Perpetuates Inequality* (New York: Oxford University Press, 2004).

<sup>9</sup> Shapiro, Thomas M., Tatjana Meschede and Sam Orso, "The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide," Institute on Assets and Social Policy, February 2013. Available at [http://iasp.brandeis.edu/pdfs/2013/Roots\\_of\\_Widening\\_RWG.pdf](http://iasp.brandeis.edu/pdfs/2013/Roots_of_Widening_RWG.pdf)

<sup>10</sup> Ryan, Doug, Emanuel Nieves, and Anju Chopra. *President Trump and Congressional Republicans Have Already Begun to Reduce Americans' Housing Choices*. Available at [http://cfed.org/blog/inclusiveeconomy/president\\_trump\\_and\\_congressional\\_republicans\\_have\\_already\\_begun\\_to\\_reduce\\_americans\\_housing\\_choices/](http://cfed.org/blog/inclusiveeconomy/president_trump_and_congressional_republicans_have_already_begun_to_reduce_americans_housing_choices/)

<sup>11</sup> *California's Housing Future: Challenges and Opportunities*.

preventing others from losing theirs to foreclosure.<sup>12</sup> (My own organization, CFED, receives support from NeighborWorks America.) NeighborWorks America's counseling programs are well-regarded in the field.

Another small, yet vital, asset-building program we need to preserve is Assets for Independence (AFI), which is run by the U.S. Department of Health and Human Services. AFI proves that with the right incentives and tools, low- and moderate-income families can and do save and make long-term investments. So far, more than 9,400 families have leveraged their savings through AFI into homeownership.<sup>13</sup> The Trump administration needs to stand with successful programs, especially those with demonstrated impacts.

In addition, proposals in Congress, and statements from the White House in support of such proposals, to undercut – if not eliminate – the regulatory authority of the Consumer Financial Protection Bureau will only embolden bad actors to reenter the lending market. The overwhelming consensus among housing experts is that predatory and unscrupulous lending practices, not borrowers and key federal policies, led to the mortgage crisis.<sup>14</sup>

Finally, reviewing the data on what did and did not cause the housing crisis is fundamental to advancing homeownership. The Affordable Housing Goals of Fannie Mae and Freddie Mac did not cause the crisis. These efforts increased the number of mortgages accessible to low- and moderate-income families by just a fraction.<sup>15</sup> Low down payment loans and the Community Reinvestment Act, sometimes mixed in with the GSEs, also did not crater the mortgage market.<sup>16/17</sup>

As both the United States and California face a decline in homeownership, policymakers and advocates need to recalibrate. One study recently predicted that the United States is already on the path to lower homeownership rates than the Golden State is already seeing.<sup>18</sup> Yet, we can and have done better. The aforementioned policies and approaches are known to work, attract multiple layers of private resources, and advance the greater good. There's little excuse not to follow a proven path. ■

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<sup>12</sup> NeighborWorks America. NeighborWorks' FY2016 National Impact. Available at <http://www.neighborworks.org/Our-Impact/NeighborWorks-Impact>

<sup>13</sup> Bolt, Chad. *Take Action Today: Let Congress Know We Can't Afford to Defund AFI*. October 18, 2016. Available at [https://cfed.org/blog/inclusiveeconomy/take\\_action\\_today\\_let\\_congress\\_know\\_we\\_cant\\_afford\\_to\\_defund\\_afi/](https://cfed.org/blog/inclusiveeconomy/take_action_today_let_congress_know_we_cant_afford_to_defund_afi/)

<sup>14</sup> Financial Crisis Inquiry Commission. *The Financial Crisis Inquiry Report*. January 2011. Available at <https://books.google.com/books?id=QIKfTVrhNfMC&pg=PAXV#v=onepage&q=XV&f=false>

<sup>15</sup> Moulton, Shawn. *Did affordable housing mandates cause the subprime mortgage crisis?* *Journal of Housing Economics*. 24 (2014).

<sup>16</sup> Ding, Lei, Roberto Quercia, and Janneke Ratcliffe. *Risky Borrowers or Risky Mortgages?* Subprime Housing Crisis Symposium, Iowa City, IA, October 11, 2008. Available at <http://ppc.uiowa.edu/sites/default/files/LeiDing.pdf>

<sup>17</sup> Reid, Carolina. *Debunking the CRA Myth – Again*. The UNC Center for Community Capital. January 2013. Available at <http://ccc.sites.unc.edu/files/2013/02/DebunkingCRAMyth.pdf>

<sup>18</sup> Acolin, Arthur, Laurie S. Goodman, and Susan Wachter. *A Renter or Homeowner Nation?* *Cityscape: A Journal of Policy Development and Research*. Volume 18, Number 1. 2016.

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# Inequality, Mobility, and the State of the American Dream

By **Kevin T. Leicht**, PROFESSOR OF SOCIOLOGY, UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN

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## KEY TAKEAWAYS

- The American Dream is on life support. Stagnant real incomes, record corporate profits, rising inequality, income, and wealth gaps between the wealthy and the rest of us, low social mobility, low retirement savings, and inflation on basic big-ticket items the middle class rely on have made life difficult for many Americans.
- The causes of this inequality are multifaceted and complex and include globalization, deindustrialization, technological change, the financialization of the economy, public policies, changing labor markets, aging populations, and educational inequality. All of these factors have contributed to the inequality we see in the United States.
- In the end, extreme inequality deprives us of a narrative for getting ahead. Economic systems need narratives to justify themselves to the population as a whole. Right now, it isn't clear what ours is exactly.

## Case Study Abstract

*The American Dream is tied to homeownership, rising wages, college education, and stable retirement in old age for a job well done. Yet this dream is in trouble, as wages for many people are stagnant or have fallen in real terms, income and wealth inequality have risen, consumption has been fueled by credit rather than rising wages, social mobility has ground to a halt, and corporations are making record profits and paying CEOs record amounts of money. The causes of this turn toward higher income and wealth inequality are many and include deindustrialization and globalization, technological change, the rising influence and role of finance, government policies favoring investment incomes over earnings, an aging population and lower birthrates, "winner-take-all" labor markets, and educational inequality. These social forces deprive average people a narrative for getting ahead that makes sense and allows people to believe in the legitimacy of the economic system.*

## Case Presentation

Is the American Dream dead? In previous research, I've posited that the American Dream has multiple meanings and lots of moving parts, but most of these are tied to the material prosperity of homeownership, steadily rising wages, college education and upward mobility for children, and a stable retirement that follows a job well done.

This dream is on life support, and here are some good reasons why:

- Real median family incomes are 15 percent lower now than they were in 1969.
  - The top 20 percent of all income earners took home 45 percent of U.S. income in 1970 and bring home 56 percent now. There is considerable evidence that almost all of that change has gone to the top five percent of U.S. income earners, thereby leaving 95 percent of us in the dust.
  - The stock market has reached record highs before and after the 2008 Great Recession, yet only 22 percent of all Americans own any stock at all.
  - Corporate profits dipped in 2008 but rapidly recovered to record levels. Productivity has risen steadily for almost 25 years. Workers' earnings have gone almost nowhere.
  - Credit card debt per household shrunk from \$12,000 in 2003 to \$10,000 now, but mostly because credit card companies have written off large swaths of debt as uncollectable.
  - The ratio of CEO to average worker pay hit 450/1 in 2007, fell after the recession, and is marching right back to where it was in 2007 and shows no signs of slowing.
  - Social mobility has ground almost to a halt; we have the lowest rates of movement across income categories and social classes of any nation in the Organization for Economic Co-operation and Development (OECD).
  - Inflation has affected basic items that middle class Americans rely on (homes, health care, child care, and state-supported higher education) in ways that have not affected prices in the rest of the economy.
- Inequality is choking off economic growth in the United States, which has been corroborated by multiple analysts across the board.
  - Wages not paid have been replaced by easily available credit.
  - There is a hidden crisis of retirement savings that looks more like a looming apocalypse because we've replaced defined pensions with defined contribution retirement plans. The mean 401K plan has \$60,329 in it. The median plan contains just \$18,000. We've culturally responded to this by "defining aging away," i.e. acting like nobody gets old, wears out, or retires. Our desire to wish away aging is suspiciously correlated with our realization that we can't afford to grow old.

The social forces that have driven inequality to unprecedented levels are complex, and different analysts provide answers to part of the puzzle. Some experts point to deindustrialization and globalization. This is the familiar part of the story. Starting in the late 1970s and going forward, American manufacturers were buffeted by competition from foreign competitors. American manufacturers were a big source of steady-paying middle class jobs, especially for workers without a college education. This competition increased the quality of goods on the market and lowered prices, but it also led to devastating declines in middle class employment, which hit the industrial Midwest and Great Lakes regions especially hard. The service and technology jobs that replaced traditional manufacturing jobs required a different set of skills. Consequently, we had a middle-aged labor force that was not in a good position to take advantage of new opportunities, and entire areas of the country that saw their labor markets collapse.

Others point to the pervasive effects of technological change. With the rise of international competition there was tremendous pressure for technological innovation. Much of that innovation has led to the development of robotics and other computerized work processes that replace lots of workers. This affected manufacturing workers most directly. While we still make things in the United States, the things we make take far fewer employees. We can outsource much of the preliminary work to others around the world.

The same is now true with many service industries, from hotel reservations to tax preparation.

In my own research, I spend a lot of time talking about financialization. When the country deregulated the financial industry, desire for new sources of profit was set loose on a population whose wages were stagnant. By the mid-1980s, one could buy cars and houses with “no money down.” You could lease cars rather than buy them. People received credit card offers through the mail. People were encouraged to take out second mortgages and use their houses as ATMs. Then the deregulated financial industry developed a way to minimize the risks of these new forms of credit. They created and expanded the Asset Backed Securities (ABS) market that allowed for the sale of securities on all kinds of consumer debt, from mortgages to second mortgages to credit cards and auto loans. The financialization of consumption severed the relationship between consumption and rising wages and allowed for record levels of profit without the accompaniment of economic improvements for everyone.

Then we get to public policy. Tax policy in the United States has been heavily tilted in favor of investment incomes over earnings. Over the course of several decades, we took basic government tax policies that attempted to tax all incomes progressively and radically shifted taxes toward wages and salaries and away from investment incomes. We did this precisely at the time that investment incomes were growing while average wages and earnings were not. We decided (culturally and economically) that investment income was “where it’s at,” even though astonishingly few Americans derive significant income from investments in the first place. And it was possible to make huge investment incomes and profits while employing very few people.

In addition, the United States and other developed nations have been hit by aging populations and lower birth rates. Thomas Piketty talks about this most directly. Wealth distributed among old people just sits there waiting to be used. If there is a vibrant and growing younger population, that wealth slowly moves in the direction of younger people and becomes active and vibrant, as the money and



assets change hands. In an economy and society that is growing older, the population that holds most of the wealth simply hangs onto it and earns more. (Some of our European and Asian neighbors have extreme versions of this problem).

Winner-take-all labor markets are another factor. Increasingly, labor markets in a lot of market niches are defined as “winner-take-all,” which means relatively few people rake in most of the rewards and very little is left for anyone else. This is true even among professional and technical workers—physicians, lawyers, scientists, college professors, and the like. In fact, income inequality has risen faster among some of these groups than it has risen in the general population. Is this a good thing? It is a bit like taking a set of seventh grade boys at age 13 and deciding who among them will be successful National Football League players and then disinvesting in everyone else. Eventually, you will face a team that trained all its players and you’re going to be at a big disadvantage.

When it comes to educational inequality, there is a growing emphasis in the labor market on skilled credentials, especially college degrees. Whether this actually means more jobs require college education is debatable, but employers are hiring job applicants with college degrees because they are available. This leaves those who can’t muster the

financial wherewithal to go to college in a bad way, especially if you’re male. We have not come up with a coherent method for training the 60 to 70 percent of the labor force that isn’t going to end up with a college diploma. That’s a lot of people to leave behind.

There is still considerable debate about how much inequality is good and at what point things start to go off the rails. Many analysts right now are concerned. Inequalities tend to be transmitted across generations. The wealthy have an easy time buying political influence that maintains their position. Those who inherit advantage think that they’ve earned it (this is called “fundamental attribution error” in social psychology). There is growing economic and cultural segregation that prevents us from understanding how the other half lives.

But the biggest thing extreme inequality does is deprive citizens of a narrative for getting ahead. What, after all, are loving parents supposed to tell their child? “Go to college, son...but make sure your roommate is the next Bill Gates!” This isn’t the future most of us envision, and without a coherent narrative for most people, the basic legitimacy of our U.S. economic system is being questioned. ■

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# The Evidence of Homeownership Education and Counseling:

## IMPROVING ACCESS TO THE AMERICAN DREAM

By **Research Utilization Division**, OFFICE OF POLICY DEVELOPMENT,  
UNITED STATES DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

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### KEY TAKEAWAYS

- Research demonstrates that homeownership education and counseling (HEC), both for those considering a home purchase and for those who are already homeowners, can provide timely, powerful support as people assess their options and make decisions.
- People benefit most from homeownership education and counseling when the support is appropriate for their needs, easily accessible, and offered early in the home-buying process.
- Research indicates that helping as many people as possible access quality counseling is the most critical factor for HEC's effectiveness. Also, social networks can also affect people's participation in HEC.
- HEC is a way to address a variety of issues facing prospective home buyers, as they often do not know or understand their financing options, and homeowners can encounter unexpected costs, struggle to maintain their initial payment plans, and encounter foreclosure rescue scams.

### Case Study Abstract

*Homeownership is complicated. Choosing and maintaining a home, as well as deciding whether to buy a home at all, can be difficult, and many people struggle to understand their choices. Homeownership education counseling (HEC) is designed to help inform consumers so they can make better qualified decisions. This submission is a summary of collected information on HEC programs to determine if they effectively reduce the risks of payment delinquency and foreclosure. Results of some of the programs researched found that participants were one-third less likely to become delinquent two years after receiving their loans, while National Foreclosure Mitigation Counseling program participants were 70 percent less likely to redefault. Overall, the research evidence demonstrates that pre-purchase and post-purchase HEC does help to reduce the likelihood of delinquency and foreclosure.*

## Case Presentation

### WHAT IS HOMEOWNERSHIP EDUCATION AND COUNSELING (HEC)?

HEC is a component of the Housing and Urban Development Act of 1968. The legislation enabled HUD to authorize public and private organizations to provide housing counseling because Congress believed that counseling was an essential complement to new mortgage insurance programs for lower-income families. HEC can help people who are considering a home purchase (“prepurchase”) and after they become homeowners (“post-purchase”). Homeownership education and counseling includes many types of support that vary in timing, method of delivery, intensity, and focus. According to HUD’s 2012 study of prepurchase counseling, nearly all (90 percent) of the participants in prepurchase HEC learn about homeownership readiness, budgeting and credit, home financing, and shopping for a home, and a smaller but still substantial proportion learn about home maintenance (63 percent) or resolving or preventing mortgage delinquency (47 percent). Post-purchase, HEC can also cover home repair, post-purchase budgeting, and decisions about refinancing and reverse mortgages.

### DO HEC PROGRAMS WORK, AND HOW?

The evidence demonstrates that HEC can help participants expand their housing searches and enjoy more options; avoid risky purchases and mortgages; lower their housing costs; improve their credit scores; save more and keep more residual income; and avoid or resolve delinquency, default, and foreclosure. HEC could also have a positive impact at a larger scale, such as by helping stabilize the neighborhoods where HEC participants live.

#### PREPURCHASE HEC

A number of prepurchase HEC programs appear to have helped borrowers avoid delinquency or defaults. In particular, a large-scale 2013 study considered nearly 75,000 borrowers: 18,258 participants in HEC programs provided by NeighborWorks America’s national network of agencies matched with 56,298 similar borrowers. Most of the participants studied were first-time

home buyers, relatively young, and earning modest incomes. According to the study, NeighborWorks participants – both first-time home buyers and repeat buyers – were one-third less likely to become 90 days or more delinquent during the two years after they obtained their loans.

A rigorous but smaller-scale 2010 study suggests that extensive, continuous pre- and post-purchase HEC by an organization with a stake in participants’ performance can substantially reduce default rates. The Indianapolis Neighborhood Housing Partnership, a HUD-approved housing counseling agency, provided low- and moderate-income households with a three-hour prepurchase class on money management, one-on-one counseling for up to two years, and a capstone eight-hour class on homebuying. Compared with similar borrowers, graduates of the program who qualified for loans with the partnership based on nonpublic, “soft” information gathered during counseling were 10.7 percentage points less likely to default. Although loans originated from 2005 to 2007, the study’s data on defaults continued through 2008, well after the beginning of the housing crash.

#### POST-PURCHASE HEC

Post-purchase HEC can help borrowers avoid delinquencies and defaults, address issues before entering foreclosure, and lower their monthly costs. The 2014 study of the National Foreclosure Mitigation Counseling (NFMC) program analyzed a sample of approximately 240,000 loans from 2009 to 2012 and found that participants were nearly three times more likely than nonparticipants to get a loan modification. In addition, among borrowers who received a modification, NFMC participants were 70 percent less likely to default again. The study also estimated that NFMC helped homeowners save \$518 million a year – an average of almost \$5,000 per client – by making both better modifications and new modifications, in addition to the savings homeowners would have achieved without a counselor’s help.

### FACTORS AFFECTING HEC OUTCOMES

The point at which consumers receive either prepurchase or post-purchase HEC does appear to make a significant difference. The National

Industry Standards for Homeownership Education and Counseling, for instance, reflect the housing industry's consensus that clients who receive earlier pre-purchase HEC have better outcomes. Evidence from a 2010 study of post-purchase counseling suggests that borrowers who receive counseling in the early stages of default may be much more likely to receive a loan modification or keep their homes compared with those who received counseling only after they were already seriously delinquent or in foreclosure. This study considered national data on homeowners who called a mortgage foreclosure hotline from 2007 to 2009, in the midst of the housing crisis.

Social networks can also affect people's participation in HEC. According to a 2015 qualitative study, working-class homeowners are more likely than middle-class homeowners to share information about the loan modification process with their social networks; middle-class homeowners are more likely to be embarrassed by their struggles with their mortgages. Similarly, a 2015 study of a New York City counseling network found that homeowners were much less likely to seek counseling services if they lived in neighborhoods with higher median home prices or lower housing burdens, even accounting for lower rates of foreclosure – perhaps it is because homeowners in these neighborhoods, which had relatively strong housing markets, underestimated the risk of foreclosure.

There is an element that does not appear to be a significant indicator. A 2013 national study of

telephone foreclosure mitigation counseling after the housing crash found that the amount of counseling homeowners received did not appear to matter; in fact, borrowers who received any amount of counseling appeared more likely to improve their delinquency status and avoid foreclosure. HUD's 2012 qualitative study of foreclosure counseling found that telephone counseling did not appear to be less effective than in-person counseling; instead, the study indicated that helping as many people as possible access quality counseling is the most critical factor for HEC's effectiveness.

## EVIDENCE TO COME

The evidence to date indicates that HEC can substantially improve prospective and current homeowners' comprehension of their choices, financial decision-making, and ability to address issues that arise with their homes or finances. The evidence also suggests that the earlier home buyers participate in pre- or post-purchase HEC, the better the outcome. ■

*\*Since the original publication of this article (Spring 2016), the preliminary findings of an HEC study of first-time homeowners has been published and posted on the HUD User website ("The First-Time Home Buyer Education and Counseling Demonstration: Early Insights"), which includes middle-income, first-time home buyers in the subject study. The full version of this article can be found in the "Research Spotlight" section of the Evidence Matters Spring 2016 housing finance issue on [www.huduser.gov](http://www.huduser.gov).*



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# Learning to Achieve the American Dream:

## EDUCATION'S IMPACT ON HOMEOWNERSHIP

By **Mark Fleming**, CHIEF ECONOMIST, FIRST AMERICAN FINANCIAL CORPORATION

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### KEY TAKEAWAYS

- The pending wave of rising educational attainment, combined with the positive influence of income growth and increased family formation, will spur an increase in homeownership demand.
- All other factors being equal, the likelihood of homeownership increases by 3 percent for those who earn a bachelor's degree over just a high school degree. The likelihood of homeownership jumps another 3 percent for those who earn a graduate degree.
- The ideal of the American Dream and the goal of homeownership will exist as long as support for higher educational attainment remains a defining tenet of American policy.
- Understanding the characteristics that influence how likely someone is to be a homeowner will help us better measure the reasons why the homeownership rate is changing and understand how to best support the pursuit of the American Dream.

### Case Study Abstract

*Homeownership continues to be the foundation of the pursuit of the American Dream. It is a critical driver of economic mobility, delivering financial and social advantages to families and entire communities. In this era of economic, technological, and societal change, understanding the state of homeownership today and what trends will influence homeownership in the future can help inform the discussions necessary to preserve homeownership opportunities for the next generation. There are many characteristics that influence the likelihood someone is a homeowner. When analyzing the homeownership rate, it's important to understand why these characteristics matter to the tenure choice decision. In this case study, we develop a model that allows us to look specifically at the importance of education to the attainment of homeownership and the American Dream.*

## Case Presentation

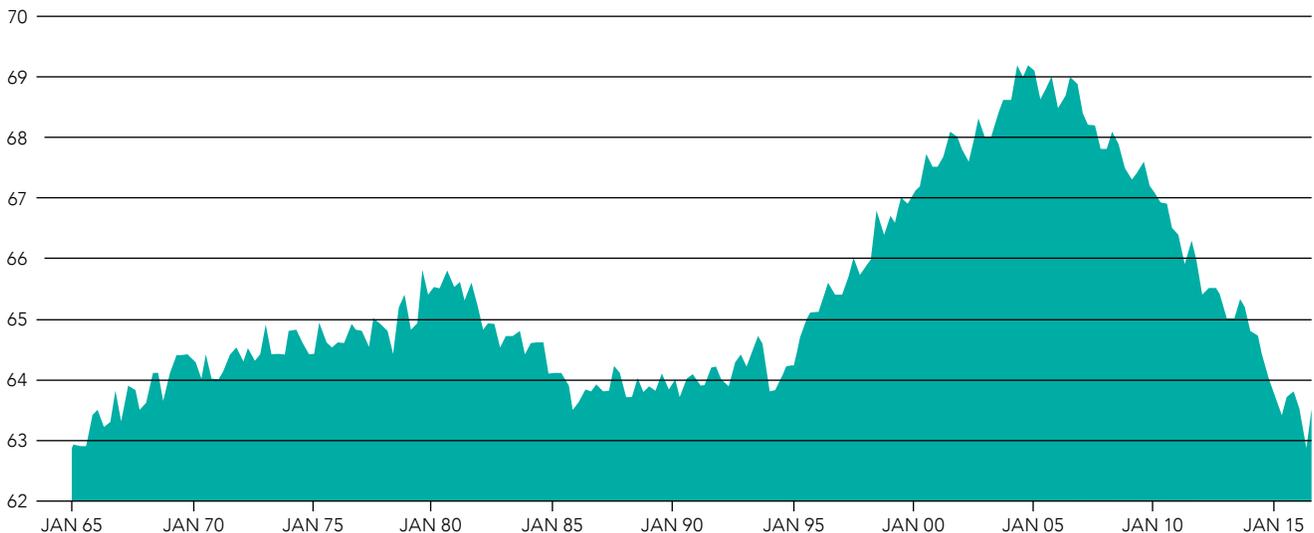
Homeownership is not just a symbol of the American Dream, but rather a real and impactful part of the economy. As the homeownership rate hits half-century lows, many are afraid that this dream is fading. However, the dream of homeownership is far from dead. Nearly 77 percent of people who responded to a recent Chase survey agreed that homeownership was a part of achieving the American Dream. After owning a home, half of respondents selected going to college, getting married, and having children as other elements that are vital to the fulfillment of that dream. Another survey confirms this sentiment, as it found that 94 percent of millennials between the ages of 20-29 are planning to buy a home.

While it may not be a surprise that homeownership remains a priority, it may come as a surprise that millennials have not been discouraged from this goal. Millennials are often referred to as a “renter generation,” because they have prioritized their education and tend to concentrate in metropolitan areas. They have – for now – chosen to share cramped apartment space with roommates over the commitment that comes with buying a home. The “American Dream” is not the mere act of owning a

home; rather, it’s an ethos or set of ideals that allows citizens the opportunity to pursue prosperity and upward mobility through hard work. In this context, homeownership is not just about shelter but a primary vehicle for wealth creation for middle-class Americans.

The concept that owning a home is a financially savvy move is not new. Our parents knew it, and their parents before them knew it. But, this idea is especially relevant for the bottom 40 percent of households, based on the income distribution in the United States. In fact, of those in this cohort who are homeowners, three quarters of their wealth comes from their home. According to the 2007 Survey of Consumer Finances, 46 percent of aggregate household wealth is residential wealth. Even during the recovery from the Great Recession, the net worth of homeowners over time outpaced that of renters, who tend to accumulate very little wealth. As you might expect, homeowners are wealthier. In dollar terms, a typical homeowner’s net worth was \$195,400, while that of a renter’s was \$5,400. The median wealth-to-earnings ratio for homeowners is almost four, but a meager 0.21 for renters. Finally, homeowners hold a staggering 97.5 percent of aggregate household wealth in the United States.

**Figure 1 IS SOMETHING RESTRICTING THE AMERICAN DREAM?**  
HOMEOWNERSHIP RATE (%)



Source: U.S. Census Bureau, Q3 2016

## CHARACTERISTICS OF HOMEOWNERSHIP

Figure 1 shows the change in homeownership rates over the past 50 years. However, it does not show the demographic, lifestyle, and economic shifts that have influenced such changes in homeownership. There are many characteristics that influence the likelihood someone is a homeowner. When analyzing the homeownership rate, it is important to understand why these characteristics matter to the tenure choice decision. First, let us dispel the common “correlation is causation” myth. The homeownership rate today only measures the percentage of homes that are owned by their occupants. Researchers frequently sub-divide this number by numerous characteristics, such as age or income. Often the homeownership gaps among these sub-divided groups are taken to mean that one characteristic makes someone more or less likely to be a homeowner.

Unfortunately, this correlation is based on a simplistic view of homeownership. It only looks at one isolated characteristic of the potential homeowner at a time. It overlooks a combination of economic and demographic factors frequently related to one another that influence the likelihood someone is a homeowner, including economic conditions, ethnicity, age, marital status, the number of children in the household, educational attainment, employment status, and income level.

For example, typically educational attainment is strongly correlated with income, as more education often leads to more income. Higher income means an increased likelihood of owning a home. Similarly, a secure job with a steady income usually indicates a greater ability to save for a down payment and a greater likelihood of access to credit. In addition, people tend to settle down in a home once they are married and decide to have children. On average, this happens to most people in their late 20s or early 30s – although millennials are pushing this age threshold increasingly higher. Other relevant factors include gender, whether one lives in an urban or rural area, and where in the U.S. one resides. In summary, it can be misleading to infer a direct causal relationship on any one of these factors without considering the others. To overcome this

dilemma, economists use a multi-dimensional analysis of relationships: “ceteris paribus,” or all other things being equal or held constant.

## THE IMPACT OF EDUCATION, CETERIS PARIBUS, ON HOMEOWNERSHIP

Millennials are going to be the most educated generation in the United States. They are the generation that has widely delayed family formation in lieu of the pursuit of higher degrees. And, despite the popular narrative surrounding millennials as “overeducated and underemployed,” a millennial with a college degree earns approximately \$17,500 a year more than a millennial with only a high school diploma. As our Homeownership Progress Index (HPRI) shows, states and markets with growing educational attainment rates often experience significant improvements in homeownership.

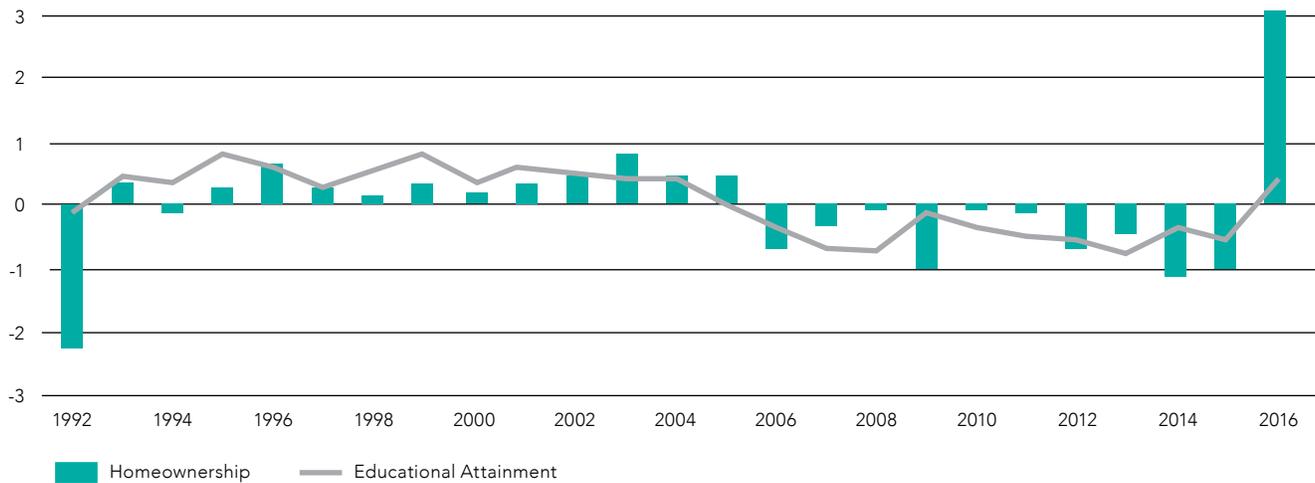
The importance of education to homeownership has only increased over time. Our HPRI shows the importance of education in relation to homeownership has almost doubled in less than 10 years. In 1997, the difference in homeownership between those with a high school degree and those with a college degree was 10 percent. In 2016, the difference increased to 21 percent. The good news is educational attainment is growing. So, it is reasonable to expect homeownership rates to grow as well. As more people achieve greater levels of education, they are able to generate higher income, and then use that higher income to buy homes.

## GET THE DEGREE, GET THE HOUSE

Our model shows that, all other factors being equal, the likelihood of homeownership increases by 3 percent for those who earn a bachelor’s degree. The likelihood of homeownership jumps another 3 percent for those who earn a graduate degree.

The good news for housing is educational attainment is increasing. Since 1991, the share of households in which at least one person has a bachelor’s degree has increased 24 percent, and is expected to increase further as millennials graduate from college and enter the workforce with improved prospects for higher-paying jobs.

**Figure 2 EDUCATION PAYS OFF**  
**YEAR-OVER-YEAR PERCENT CHANGE**



Source: IPUMS CPS, 2016

Figure 2 shows the change in homeownership rates caused, all else held constant, by the change in the attainment rate of bachelor’s degrees. Between 1992 and 2005, the increasing share of individuals earning bachelor’s degrees led to a 2.7 percent increase in homeownership. Between 2005 and 2015, partially in response to the Great Recession and slow economic recovery, millennials have been staying in school. Consequently, the educational attainment rate, which measures the completion of degrees, declined. All else held constant, this caused modest year-over-year declines in the homeownership rate. In 2016 (the most recent year with available data), a jump in the educational attainment rate drove a 3 percent year-over-year gain in homeownership.

**EDUCATION HELPS ACHIEVE THE AMERICAN DREAM**

The causes for the rise and fall of the homeownership rate are complicated and include shifts in demographics, lifestyle choices, and economic factors. All else held constant, it is apparent that educational enlightenment is critically important to achieving homeownership. According to the PEW Research Center, the good news is that 63 percent of millennials value a college

education or plan to get one. Of that number, 19 percent have already graduated from college and the remaining 44 percent plan to graduate from college. Approximately 27 percent of millennial women and 21 percent of millennial men have college degrees. This is in stark contrast to only 20 percent of Generation X women and 18 percent of Generation X men. The comparison to baby boomers is even more dramatic, as only 14 percent of women and 17 percent of men have degrees. Based on our model and analysis, the pending wave of rising educational attainment, combined with the positive influence of income growth and increased family formation, will spur an increase in homeownership demand.

Owning a home also plays a role in providing social stability and financial security. It is a major component of the U.S. economy and significant contributor to the upward mobility of its citizens. The ideal of the American Dream and the goal of homeownership will exist as long as higher educational attainment is a goal in our society and defining tenet of American domestic policy. ■

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# Rebuilding Pathways to Homeownership:

## POLICY PRIORITIES FOR MILLENNIALS AND THE MIDDLE CLASS

By Reid Cramer, SENIOR FELLOW, NEW AMERICA

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### KEY TAKEAWAYS

- Policies are needed to help families strengthen their financial position to better prepare for homeownership. This requires supporting families' efforts to increase their incomes, save for a down payment, and maintain or repair credit scores – all of which can limit the risk of future loan defaults.
- Policymakers need to balance the objectives of making sure mortgage credit is available to worthy borrowers and setting standards to protect consumers in the financial services marketplace.
- Current policy in place to support homeownership too often fails to help younger households become better positioned financially. Homeownership has declined in the wake of the Great Recession, particularly among millennials.

### Case Study Abstract

*Policymakers need to balance the objectives of making sure mortgage credit is available to worthy borrowers, setting new standards to protect consumers in the financial services marketplace, and helping families strengthen their financial position to better prepare for homeownership. Further policy solutions will be required to address the inequities in current policy, and to re-examine how access to housing finance can embrace the diversity of America. If the rising cohort of young adults cannot improve their balance sheets by increasing their savings and lowering their liabilities, they will be denied access to one of the most historically powerful asset-building tools: appropriate mortgage financing. Policy supports in place to advance homeownership often fail to help younger households become better positioned financially. Overall, homeownership has declined in the wake of the Great Recession, particularly among millennials who should be entering their prime home-buying years.*

## Case Presentation

Becoming a homeowner has long represented a symbolic milestone on the road to adulthood. Yet in the wake of the Great Recession, this archetypal symbol of the American Dream has become increasingly elusive. Our national homeownership rate has markedly declined. One illuminating feature of this trend is the diminished incidence of ownership among the millennial generation, the oldest of which should be entering their prime, first-time home-buying years.

It's true that in recent years, young adults are marrying at lower rates and putting off child rearing, which lessen the drive for homeownership. They also appear to prefer living in greater proximity to urban amenities, making suburban options less attractive, and are living longer with friends or family, rather than living alone. Still, coming of age after the bursting of the housing bubble appears to have fundamentally altered their material prospects. They earn less than what their parents made at a comparable age and carry higher levels of student loan debt. Through changes in preference or circumstance, it is likely that today's rising generation of Americans has a more idiosyncratic relationship with homeownership than their elders.

This is not a crisis per se. Homeownership is not always the right choice for everyone, but the slowdown of home buying among young adults is potentially troubling for several reasons. First, pursuing homeownership early is a key factor in being able to build up financial assets over the course of life. (Emmons and Noeth 2014) Homes are often the largest item on a family's balance sheet. (Key 2014) If other avenues to accruing wealth aren't created, the current – and lower – trajectory of homeownership among millennials will remain a drag on the generation's finances over the long term. Second, homeownership has been a way for families to access valuable services. It is the residential stability – not just the fact of ownership – that delivers additional benefits. Third, homeownership appears to be an enduring aspiration of many young families, who see it as a primary marker of achievement in and of itself. (Fannie Mae 2014) While there are risks and responsibilities to consider with ownership, its

decline should be a concern for policymakers, who should strive to create viable pathways for those interested in pursuing this opportunity.

### PUBLIC POLICY ISSUES IN PLAY

The ability to become a homeowner in the United States is dependent upon several factors, including the ability to make a down payment, qualify for a mortgage, find a house that is affordable, and consistently make loan payments from income over an extended time horizon. All these elements must come into alignment for a family to be able to responsibly purchase and maintain ownership of a home. Since the recession, each of these factors has become more challenging. Furthermore, few of the current policy-supports in place to advance homeownership are well positioned to help younger households.

One of the biggest policy levers in use is the mortgage interest deduction, which costs taxpayers about \$74 billion a year. But this subsidy does not help Americans afford homes and prepare for their first purchase; rather, its benefits are reaped only after people have become homeowners. (Fischer and Huang, 2013) Notably, millennials as a group are increasingly likely to have lower incomes, thereby putting them at a distinct generational disadvantage in benefiting from the mortgage interest deduction (MID). (Joint Center for Housing Studies 2014) According to the Center on Budget and Policy Priorities, "77 percent of the benefits from the mortgage interest deduction [go] to homeowners with incomes above \$100,000, almost none of whom face severe housing cost burdens." (Fischer and Huang 2013) Furthermore, only about 31 percent of taxpayers itemized their tax deductions in 2012, so this policy misses many people who might benefit from it. (Urban-Brookings Tax Policy Center 2014)

Since the advent of the Federal Housing Administration in the 1930s, one of the defining characteristics of the U.S. housing market has been the widespread availability of mortgage financing. This was a primary force behind rising rates of ownership in the second half of the 20th century. Unfortunately, with lax oversight, the oversupply of credit played a role in creating the conditions that

precipitated the Great Recession. Policymakers have not addressed the most basic questions of what the housing finance system will look like in the decades ahead. The government-sponsored enterprises responsible for providing housing financing, Fannie Mae and Freddie Mac, remain in government conservatorship. There appears broad consensus that this is unsustainable, but Congress has yet to act on establishing a new set of rules, and the new administration does not appear poised to provide a clear path forward.

## CHALLENGES TO ADDRESS

Given the prevailing uncertainty in the housing finance system, it remains to be seen if public policy can be crafted to help young families become homeowners in sustainable and responsible ways. Policymakers will need to balance the objectives of making sure mortgage credit is available to worthy borrowers and setting new standards to protect consumers in the financial services marketplace. Regulatory oversight of financial services is needed to ensure high-quality mortgages are offered with appropriate underwriting standards. Eliminating the availability of predatory financial products will go a long way to mitigating the high levels of risk that became apparent during the recent housing crisis. These are tasks being assumed by the Consumer Financial Protection Bureau, which will likely have to navigate many future political obstacles to remain effective in its mission.

Another challenge to address is ensuring that there is sufficient supply of affordable homes accessible to first-time buyers with modest resources. In some cases, it may require expanding the models of housing ownership, to include cooperatives and shared equity projects.

Still, much of the work to be done is on the demand side: families need to strengthen their financial position to better prepare for homeownership. This requires supporting families' efforts to increase their incomes, save for a down payment, and maintain or repair credit scores, all of which can limit the risk of future loan defaults. While we have seen the job market tighten in recent years, which has helped median incomes rise, earnings remain

below pre-recession levels. In addition to having lower and unstable income streams, millennials have higher levels of debt, especially in the form of student loan debt, compared to previous generations of young people. In 2010, 41 percent of households under age 30 held student loan debt, compared to 30 percent in 2004, and the amount of debt has increased. (Herbert 2013)

At the same time, as less money is being saved by millennials, more money is being required by lenders for a down payment. If the rising cohort of young adults cannot improve their balance sheets by increasing their savings and lowering their liabilities, they will be denied access to one of the most historically powerful asset-building tools – appropriate mortgage financing. Further policy solutions will be required to address the inequities in current policy and to re-examine how access to housing finance can embrace the diversity of America. Responding to these challenges can play a constructive role in expanding the opportunity of ownership in America.

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# Maryland SmartBuy Program:

## AN INNOVATIVE NEW PATH TO HOMEOWNERSHIP FOR BUYERS WITH STUDENT LOANS

By **Sergei Kuzmenchuk**, CHIEF FINANCIAL OFFICER, MARYLAND DEPARTMENT OF HOUSING  
AND COMMUNITY DEVELOPMENT

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### KEY TAKEAWAYS

- The Maryland Department of Housing and Community Development implemented an innovative homeownership program to help credit-qualified home buyers with student loan obligations buy their own homes. Without this program, many potential home buyers would struggle with access to homeownership.
- The program benefits the home buyers, the neighborhoods, and the department, as it fulfills its mission of providing affordable and sustainable financing for qualified home buyers while stabilizing communities.
- The program was approved in the 2016 legislative session through legislation introduced by Gov. Larry Hogan.

### Case Study Abstract

*If you have not been keeping up with changes to underwriting requirements for residential mortgage loans, you may not be aware of recent requirements for mortgage companies to use student loan repayment obligations as a reduction in a home buyer's ability to qualify for a higher mortgage loan. This change alone, as well-intentioned as it may be, caused many previously-qualified home buyers to be priced out of the home-buying market.*

*The Maryland Department of Housing and Community Development developed a program that effectively tackles this impediment to homeownership. Program participants must buy one of the department-owned homes to qualify for very advantageous financing through the Maryland Mortgage Program. In exchange, the participants have their student loans paid off at home purchase, and if they live in the home for 5 years or longer, the additional mortgage loan used to pay off the student debt will be fully forgiven.*

## Case Presentation

The Maryland Department of Housing and Community Development financed more than 10,000 loans over the last five years, in addition to funding thousands more loans since its inception for primarily first-time home buyers in the state of Maryland. Through prudent underwriting requirements and conservative financial management, the department has been able to ensure a successful and sustainable homeownership experience. A small percentage of homes end up in foreclosure and result in the department taking ownership of certain homes with deferred maintenance issues. The department then restores these homes to be owner-occupant-ready and markets them to creditworthy individuals who have student loan obligations that prevent them from qualifying for mortgage financing.

Known as the Maryland SmartBuy program, this innovative approach was designed to allow the department to sell its own homes and provide unique mortgage financing benefits to the buyers of these properties. To implement this program, the department partnered with Fannie Mae, private mortgage insurance companies, its extensive network of private originating lenders, real estate agents, title companies, and its master loan servicer, U.S. Bank. The department renovates and offers its homes for sale at fair market value using its real estate partners, Long & Foster and Cummings & Co. Up to 15 percent of the purchase price of these homes is offered to pay off student loans for otherwise qualified home buyers.

This is a win for home buyers, as they swap their student debt obligations for this newly added capacity to borrow funds for the purchase of a home. This is also a win for our neighborhoods. Since the values of these homes are not discounted by the 10-20 percent typical of other bank-owned property sales, the neighborhood benefits from

stable home valuation (the current market value at the time of appraisal) and from putting owner-occupants in these otherwise empty homes. Finally, this is a win for the department, as it accelerates sales of its real estate owned properties, which are non-revenue but expense-generating assets due to maintenance costs. By substituting them with performing loans, the department will benefit from revenue generated over time, which will repay the amount of sale proceeds used to pay off student debt at the time of home purchase.

This program augments the department's mission-centric standing in the community without causing negative credit implications for its highly-rated housing program portfolios, as attested to by Moody's Investors Service in its publication dated Dec. 12, 2016, "Maryland Community Development Administration: Maryland CDA's Student Loan Homeownership Program Is Credit Neutral."

Since the official commencement of the program in November 2016 to the end of March 2017, the department sold seven homes in six counties with an average purchase price of \$199,000. For each of the buyers, we offered a \$5,000 down payment and closing cost assistance and a zero percent deferred loan. Plus, on average, we used 9 percent of sale proceeds to pay off student loans. Any amount the department uses to pay off a student loan is recorded as a second lien loan on the home, forgivable over five years. The forgivable loan requirement was put in place to prevent "home flipping" and to ensure that only home buyers who intend to own their homes for longer terms qualify for this financial assistance package. ■

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Sergei V. Kuzmenchuk joined the Maryland Department of Housing and Community Development ("the Department") as its Chief Financial Officer in June of 2015 after serving as Chief Financial Officer at the District of Columbia Housing Finance Agency (the "DCHFA") since October 2008. Prior to joining the DCHFA, he served as the Department's Deputy Director of Finance for the Community Development Administration ("CDA") from August 2000 until January 2006, and Director of Finance for CDA from January 2006 until October of 2008.

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# Fostering Growth and Opportunity in California for a Strong Middle Class

By **Loren Kaye**, PRESIDENT, CALIFORNIA FOUNDATION FOR COMMERCE AND EDUCATION

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## KEY TAKEAWAYS

- Promising economic figures have catapulted California's gross domestic product to the top six among nations. But even though the state has experienced huge wealth and employment gains, millions of families cannot reach the California dream and are struggling financially.
- Poverty is not limited to rural and inland California. Much of the poverty in coastal California is a function of housing costs that distort expenses of wage earners.
- Even when employees can find affordable housing away from the metropolis, the long and slow commute adds yet another financial burden and social stress. The state sorely needs increased housing supply and more infrastructure investment.
- Increasing opportunity is within reach of the state's leaders. There are five key goals that lawmakers should focus on to ensure economic mobility is possible for more Californians.

## Case Study Abstract

*Increasing opportunity in California will require the state's lawmakers to focus on several key areas that will address lingering problems that inhibit economic mobility and shared prosperity. Namely, focus should be placed upon investing in transportation and water infrastructure, increasing housing supply, making energy more affordable, updating labor laws and reducing litigation, and investing in education and a skilled workforce. Without broad investments and steps to enlarge the economic pie for the middle class, millions of families will not be able to reach the California dream and will continue to struggle financially.*

## Case Presentation

From a distance, it seems the California economy couldn't do any better. Our gross domestic product is in the top six among nations. We lead states in economic output per capita, and statewide employment growth is the envy of the nation. We're creating wealth faster than at any time since the Incan conquest.

But behind all this lurks a complicated mix of the prosperous and the desperate. Even among huge wealth and employment gains, millions of families cannot reach the California dream and are struggling financially. For example, one in three Californians receives subsidized health care through Medi-Cal. More than 3.3 million schoolchildren receive subsidized school lunches – about half of total public school enrollment.

Economic distress has a clear geographical dimension. When examining the 36 counties in rural, mountain, and Northern California, the aggregate unemployment rate is 6.6 percent. If rural California were a separate state, its unemployment rate would be the highest in the country. On the other hand, unemployment in the 22 coastal and metropolitan California counties is just 4.8 percent, one of the lowest of all industrial states. Rural California also suffers more widespread poverty than its coastal and metro neighbors. The official poverty rate is higher, as is enrollment in Medi-Cal.

But poverty is not limited to rural and inland California. Much of the poverty in coastal California is a function of housing costs that distort expenses of wage earners. Zillow reports that renters in the Los Angeles metropolitan area pay 48 percent of their monthly income for the median rent. Almost half of working-age adults in Los Angeles County double up with roommates in housing units.

According to analysis by the Milken Institute, median rentals of one-bedroom apartments exceed 30 percent of median income in the San Francisco Bay Area, Los Angeles, and San Diego. Even when employees can find affordable housing away from the metropolis, the long and slow commute adds yet another financial burden and social stress. The path to economic success is a good education.

But yet again the California fault lines divide educational attainment. The Milken Institute has also found that a region's per capita economic output is closely tied to its educational attainment. The regions with the top educational attainment nationally are in the San Francisco Bay Area, and notably have among the top-ranked GDP per capita. Just 80 miles inland, five regions in the San Joaquin Valley are in the bottom 10 of educational attainment, and scrape the bottom in per capita GDP.

Still, economic success breeds its own problems, even in metro California. A high cost of living is driven in large part by housing shortages and long commutes, which in turn can be addressed only through increased housing supply and more infrastructure investment. Increasing opportunity and offering everyone a slice of the pie is within reach of state leaders. Lawmakers should start with these five goals:

**1. INVEST IN TRANSPORTATION AND WATER INFRASTRUCTURE.** California's road financing system cannot keep up with the state's needs. Our fuel-stingy auto fleet cleans our air but starves our roads. The result is a \$59 billion shortfall in deferred road maintenance. Lawmakers must heed the governor's call to ramp up highway and transit funds and modernize fee-for-service road financing. State leaders must also maintain momentum on the Delta conveyance system, which is critical to satisfying our long-term urban and agricultural water needs.

**2. INCREASE HOUSING SUPPLY.** The only solution to the high cost and severe shortage of housing is to increase supply, but California's environmental and land use laws undermine this imperative. Policymakers now favor more housing in dense, urban areas, but have not, in turn, reduced the inevitable permitting, zoning, and litigation burdens, such as in the California Environmental Quality Act. Lawmakers should take every opportunity to expand our housing footprint, or housing costs will continue to stifle economic growth for future generations.

**3. MAKE ENERGY MORE AFFORDABLE.** Higher energy prices will continue to add to California's cost of living and detract from our competitiveness unless climate change laws incorporate more cost-

effective, market-based approaches to reduce greenhouse gas emissions. In order to show leadership that climate change regulations can be both effective and affordable, we must adopt a cap-and-trade mechanism to replace command-and-control regulations. A regionalized electric utility marketplace can partly mitigate the higher costs of renewable power.

#### 4. UPDATE LABOR LAWS AND REDUCE LITIGATION.

California's employment laws and regulations have not kept pace with the evolution of the workplace, technology-based services, or workers' needs. State leaders must update archaic regulations that hinder new workplace models that utilize independent contractors, discourage flexible, family-friendly work design, and put storefronts at a disadvantage vis-à-vis digital presence. Where there are legitimate disputes, we must protect the ability of employers and employees to resolve those disputes expeditiously and inexpensively through arbitration.

#### 5. INVEST IN EDUCATION AND A SKILLED

**WORKFORCE.** Besides the weather, California's greatest competitive advantage is our skilled workforce. The Legislature should continue improving state support for universities and colleges to restore our qualitative advantage, and continue investment in high school work-based learning initiatives, which allow students to apply their classroom learning in a professional setting to gain real-world experience and relevance.

California is a wealthy state, boasting great natural and intellectual resources. It is within the power of state leaders to foster growth and increase opportunity, no matter the crosscurrents blowing in from Washington. ■

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Loren Kaye was appointed president of the California Foundation for Commerce and Education in January 2006. The foundation is affiliated with the California Chamber of Commerce and serves as a "think tank" for the California business community. He was also a gubernatorial appointee to the state's Little Hoover Commission, charged with evaluating the efficiency and effectiveness of state agencies and programs. Kaye served in senior policy positions for Govs. Pete Wilson and George Deukmejian, including Cabinet Secretary to the Governor and Undersecretary of the California Trade and Commerce Agency.

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#### BACKGROUND

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