Housing

CALIFORNIA'S FUTURE

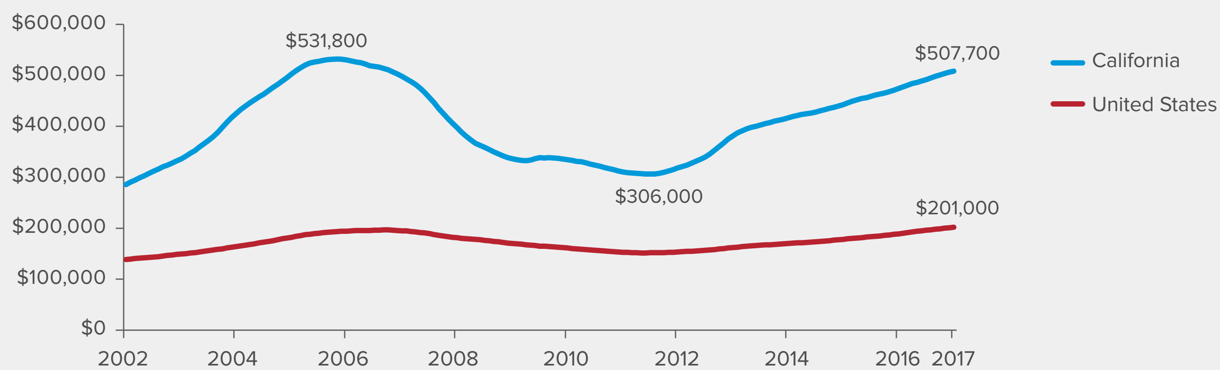
JANUARY 2018

California's housing challenges continue

California home values and rents remain the most expensive in the nation, and they continue to rise. As of August 2017, median home values climbed 7.1 percent over the year to reach $507,700. Rents have also increased sharply, driven by exceptionally strong demand. New housing construction is increasing at a slow and steady pace but remains well below pre-recession levels and far short of demand.

Gains in home values have been uneven across the state, but high rents and rising prices place housing out of reach for many—leading in some cases to homelessness. The state's affordability problem has been aggravated by slow growth in household income. According to the PPIC Statewide Survey (May and September 2017), 47 percent of Californians—including 61 percent of renters—say housing costs are a financial strain on themselves and their families. The rising cost of housing has emerged as a threat to the state's future economy and the well-being of its citizens, pushing the debate over housing to the center of state and local politics.

MEDIAN HOME VALUES: BOOM, BUST, AND RECOVERY



SOURCE: Zillow.

NOTE: Values in nominal dollars from January 2002 to August 2017.

Housing values keep rising, but the pace is uneven

- **California home values have increased substantially since the housing bust.**
  The state's median home value is up 66 percent from its low in 2012; at $507,700, it is within 5 percent of the previous peak in 2006. In five Bay Area counties (San Francisco followed by San Mateo, Santa Clara, Alameda, and Marin) and in San Diego and Los Angeles Counties, values are now above previous highs. Over the past six years, some of the sharpest gains have occurred in counties that had the worst busts, including 113 percent in San Joaquin, 92 percent in Sacramento, 84 percent in San Bernardino, and 74 percent in Riverside. But values in those counties are still 13 to 22 percent below their peaks. In 15 counties, mostly in the San Joaquin Valley and the Central Sierra, prices remain more than 20 percent below their peaks.
- **Foreclosures have dropped to their lowest level in years.**
  California's total foreclosure activity (which includes foreclosure starts, scheduled foreclosure auctions, and bank repossessions) declined about 80 percent from August 2012 to August 2017. Foreclosure starts are at about 6.6 percent of their 58,858 peak in May 2009 and are below pre-crisis levels.
- **New construction permits are increasing.**
  Low vacancy rates, rising prices, and low interest rates are boosting housing starts. New residential construction permits are set to exceed 100,000 in 2017—up from 33,000 in 2009 but still far below the 200,000 units permitted

annually from 2003 to 2005. Fueled by strong rental demand, multifamily residential permits began to show robust gains in 2010; however, the pace slowed considerably over the past couple of years. Meanwhile, construction jobs are growing faster than employment in most other sectors.

MEDIAN HOUSING VALUES HAVE RISEN IN CALIFORNIA'S 15 MOST POPULOUS COUNTIES

	Peak (2006 or 2007)	Low (2011 or 2012)	Current (August 2017)	Peak to current	Low to current
Alameda	$629,600	$403,500	$782,900	24%	94%
Contra Costa	$615,000	$308,200	$575,400	-6%	87%
Fresno	$293,800	$135,400	$226,300	-23%	67%
Kern	$270,800	$120,300	$194,700	-28%	62%
Los Angeles	$560,100	$354,300	$572,900	2%	62%
Orange	$708,800	$454,400	$689,800	-3%	52%
Riverside	$424,900	$199,800	$347,300	-18%	74%
Sacramento	$385,900	$175,400	$336,600	-13%	92%
San Bernardino	$379,000	$169,900	$313,000	-17%	84%
San Diego	$543,600	$347,000	$552,400	2%	59%
San Francisco	$830,700	$658,400	$1,234,800	49%	88%
San Joaquin	$411,100	$151,400	$322,300	-22%	113%
San Mateo	$816,300	$599,400	$1,199,300	47%	100%
Santa Clara	$751,700	$569,400	$1,057,600	41%	86%
Ventura	$632,200	$376,900	$566,700	-10%	50%
California	**$531,800**	**$306,000**	**$507,700**	**-5%**	**66%**

SOURCE: Zillow.

NOTES: In nominal dollars. For most counties, the pre-recession peak occurred in 2006 or 2007, and the low in 2011 or 2012.

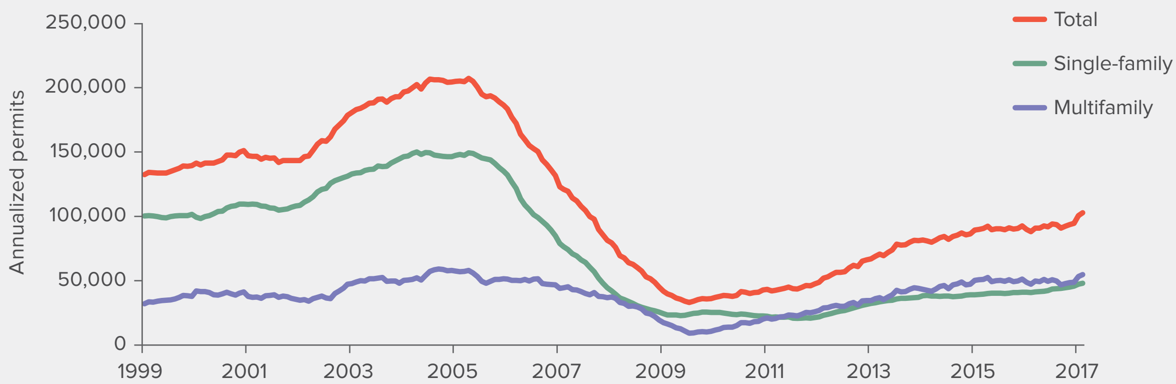
Housing remains expensive for most people

- **Californians spend disproportionate shares of their income on housing.**
  Among homeowners with mortgages, median monthly housing costs are 47 percent higher in California than nationwide. California renters pay 40 percent above the nationwide median. Yet California's median household income is only 18 percent higher than the nationwide median. This means that the share of Californians with excessive housing costs is quite high: 30 percent of mortgaged homeowners and 46 percent of renters spend more than 35 percent of their total household income on housing, compared with 21 percent and 40 percent, respectively, nationwide.

- **Housing is especially unaffordable in coastal areas, where two-thirds of Californians live.**
  In the second quarter of 2017, nine of the nation's ten least affordable major metropolitan areas (with populations of 500,000 or more) were in California. The San Francisco metropolitan area (San Francisco, San Mateo, and Marin Counties) was the least affordable major market; the Los Angeles, Orange County, San Jose, Santa Rosa, Ventura, San Diego, Oakland, and Stockton metropolitan areas were also in the top ten. In most of these areas, fewer than one-fifth of households could afford a median-priced home. The metropolitan areas of Salinas (Monterey County), Santa Cruz–Watsonville, Napa, and San Luis Obispo–Paso Robles were the nation's least affordable smaller housing markets.

- **Inland home prices are lower.**
  Despite price increases, housing is relatively affordable in many California inland areas. In the Redding, Bakersfield, and Chico metropolitan areas, families earning the area's median income could afford more than 55 percent of homes sold in the second quarter of 2017. In Sacramento and the Inland Empire, 38 percent and 35 percent of homes sold were affordable to families at the median income.

NEW HOME CONSTRUCTION PERMITS ARE ALMOST BACK TO 2007 LEVELS



SOURCE: US Census Bureau, Building Permits Database.

NOTE: July 1998 to July 2017.

- **Rents are high and rising.**
  California has six of the nation's eleven most expensive large metropolitan rental markets: San Francisco is number one, followed by San Jose, Oakland, Orange County, San Diego, and Los Angeles. Since 2015, rents have increased more than 40 percent in the San Francisco, San Jose, and Oakland metropolitan areas. Estimated median rent for a two-bedroom apartment ranges from $1,798 in Los Angeles to $3,377 in San Francisco.
- **Vacancies are low.**
  Low vacancy rates have contributed to the tightness of the rental market. In 2016, California's homeowner residential vacancy rate was 1.3 percent compared to 1.8 percent nationwide. Meanwhile, the rental vacancy rate was 3.3 percent, 2 percentage points lower than in 2010 and far below the 5.9 percent nationwide rate.
- **Homeownership rates have fallen.**
  Over the past decade, homeownership rates, already much lower in California than in the rest of the nation, declined more sharply: to 53.6 percent of occupied units in 2016 (from 58.6% in 2004), compared with 64.3 percent in the rest of the country. Owner-occupied units fell by about 133,500, while rented units increased by more than 877,000. Much of the increase in rental units has occurred among formerly owned single-family detached housing units. California and national homeownership rates are the lowest in more than a dozen years.
- **Homelessness is widespread.**
  The US Department of Housing and Urban Development estimates that on a single night in January 2016, about 118,000 individuals in California were homeless—21 percent of the national total. Only 34 percent of California's homeless are in shelters or other residential programs—the lowest rate in the nation. The largest number of homeless people live in Los Angeles County, but homelessness affects most counties, even small and rural ones.

Looking ahead

As the state's population grows, housing demand continues to increase. California needs short- and long-term policies that improve housing affordability and remove unnecessary barriers to expanding supply, while meeting environmental goals. State efforts must interact with local land-use and zoning policies; this means that addressing California housing problems will take many years of sustained work and cooperation between state and local officials.

State and local land-use policies should encourage more housing. California's tight housing market reflects not only a scarcity of developable land but also an array of policy choices and regulations. Promotion of commercial development, such as tax incentives for businesses that relocate, should be balanced by policies that encourage new housing. Restrictive zoning and planning regulations can depress housing supply and increase housing costs. In 2017, the state legislature passed a series of bills to incentivize housing production by promoting higher density, speedier regulatory permitting, streamlined housing approvals, and the zoning of land for housing. For the first time, local jurisdictions could face substantial penalties, including litigation, for failing to plan adequately for future housing needs.

State and local authorities should boost the supply of affordable housing. Historically, the state has funded affordable housing programs through the sale of general obligations bonds and from redevelopment funds. But California has not passed a general housing bond since 2006, when Proposition 1C provided $2.85 billion, and redevelopment agencies were dissolved during the recession. In 2017, the governor signed the Building Homes and Jobs Act, which imposes a $75 fee on real estate transaction documents, excluding commercial and residential real estate sales, to provide ongoing funding for affordable housing. The legislature and governor also agreed to a $4 billion general obligation bond for affordable housing programs, subject to approval by voters in November 2018. According to the PPIC Statewide Survey (May and September 2017), strong majorities favor an affordable housing bond; fewer support a real estate transaction fee.

California should expand housing options for homeless individuals and families. Reducing homelessness in California requires coordinated investments, policies, and programs at the federal, state, and local levels, as well as collaboration across sectors (housing, health, and social services). In 2016, the governor signed legislation requiring state agencies and departments that provide services to the homeless or those at risk of homelessness to incorporate core components of the Housing First model. This approach prioritizes getting homeless people into housing and providing services as needed.

Balancing environmental goals with housing development will be a challenge. California has passed legislation to encourage local land-use planning that reduces driving—and lowers harmful emissions. The goal is to coordinate new housing development with current and planned transportation networks. Infill (new construction in built-up areas) is one way to achieve this goal, but there is a trade-off. In the past, much of California's most affordable new housing was built on vacant land at the edge of urbanized areas. Infill development tends to be more expensive and usually produces fewer units. Identifying water sources for new development is also an issue in some parts of the state.

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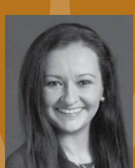

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