PPIC

Housing

CALIFORNIA'S FUTURE

JANUARY 2020

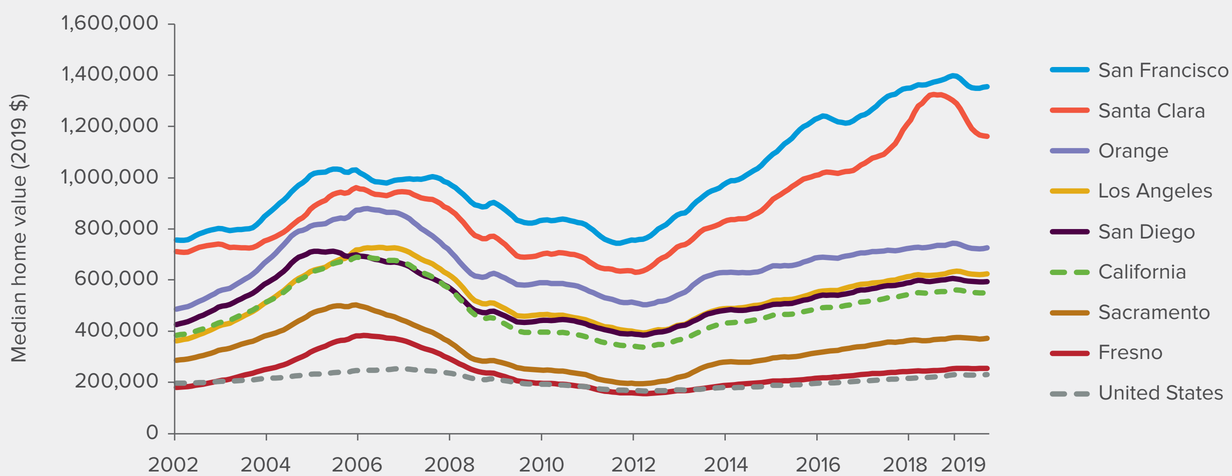
California's housing challenges have widespread effects

The high cost of housing has emerged as a threat to California's future. Many Californians see homelessness and housing costs as the state's most important challenges, according to the PPIC Statewide Survey (September 2019). This is not surprising, considering that California has the second-highest homelessness rate in the nation and ranks near the top in cost-burdened households—second among homeowners and third among renters. Indeed, according to the California Association of Realtors, only 31 percent of households can afford to buy a median-priced home in California in the third quarter of 2019, 25 percentage points lower than the nation's average. What is more, California has one of the highest poverty rates in the nation when housing costs are accounted for.

The governor and the state legislature have taken steps to spur housing production and address homelessness. The 2019–20 state budget includes $1 billion to address homelessness, a historic $1.75 billion investment in new housing, and incentives for cities to approve new home construction. The governor signed 18 bills in 2019 designed to help jump-start housing production, including major legislation (SB 330) aimed at removing local barriers to housing construction and speeding up new development; he also signed a statewide rent control measure. At the same time, several local jurisdictions have dramatically expanded funding for affordable housing and homelessness prevention and services.

There are no quick fixes to California's housing crisis, which has been decades in the making. State efforts to improve housing affordability, increase housing supply, and address homelessness must interact with local policies. This means that identifying and implementing effective strategies will require sustained cooperation between state and local stakeholders.

HOME VALUES VARY WIDELY ACROSS THE STATE



SOURCE: Zillow.

NOTE: Values for selected counties, the state, and the United States are reported in September 2019 dollars from January 2002 through September 2019.

Housing remains expensive for most Californians

- **California home values have risen significantly since the recession…**
  The state's median home value remains the second highest in the nation (after Hawaii) at $550,800 as of September 2019, 2.4 times higher than home values nationwide. Statewide, home values in real (inflation-adjusted) terms are 63 percent higher than the March 2012 low ($337,900), much greater than the nationwide increase (39%). In real terms, the majority of counties have not surpassed their pre-recession peaks. Indeed, home values in eight counties,

including Kern, Monterey, and Merced, remain more than 35 percent below their peaks. However, in three San Francisco Bay Area counties (San Mateo, San Francisco, and Santa Clara), home values are 20 to 30 percent above previous highs. If we look at home values in nominal terms, 16 counties have home values above previous highs.

- **…but the pace has slowed.**
  In the first nine months of 2019, year-over-year growth was on average 2.4 percent, compared to 7.6 percent on average in the first nine months of 2018. Moreover, since July 2018, home values in California have been growing at a slower pace than home values in the nation as a whole; since March 2019, home values are trending down in several counties, including Santa Clara, San Mateo, Alameda, and Sonoma.

- **Rents are high and rising.**
  California has six of the nation's fifteen most-expensive large metropolitan rental markets: San Francisco (number one), San Jose, Oakland, Orange County, San Diego, and Los Angeles. Since 2015, rents have risen anywhere from 36 percent to 60 percent in nominal terms in these areas. According to US Department of Housing and Urban Development (HUD), the median rent for a two-bedroom apartment in these areas ranges from $2,113 in Los Angeles to $3,477 in San Francisco. Statewide, inflation-adjusted rents have risen by 13 percent since 2012, compared with 8 percent nationally, according to Zillow estimates.

- **Californians spend disproportionate shares of their income on housing.**
  Among homeowners with mortgages, median monthly housing costs are 50 percent higher in California than in the nation as a whole. California renters pay 44 percent above the nationwide median—while California's median household income is only 22 percent higher than the nationwide median. This means that the share of Californians with excessive housing costs is quite high: 38 percent of mortgaged homeowners and 55 percent of renters spend more than 30 percent of their total household income on housing, compared with 28 percent and 50 percent nationwide.

- **Housing is especially unaffordable in coastal areas, where two-thirds of Californians live.**
  Eight of the ten least-affordable major metropolitan areas in the nation in the third quarter of 2019 were in California, according to the National Association of Home Builders. Seven of these areas are along California's coast; fewer than one in four households could afford a median-priced home in these metros. The San Francisco metropolitan area (San Francisco and San Mateo Counties) was the least affordable: only 8.4 percent of the homes sold were affordable to families earning the area's median income of $133,800. Metropolitan Los Angeles, Orange County, San Jose, San Diego, Ventura, Oakland, and Stockton, were also in the top 10. A few areas remain relatively affordable. For example, in metropolitan Bakersfield, 57.7 percent of homes sold were affordable to median-income families.

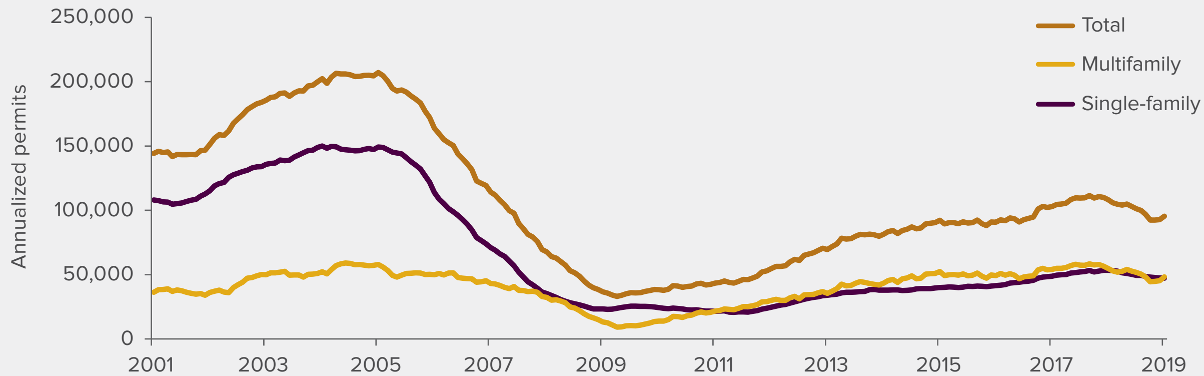
Supply shortages will continue to put upward pressure on home prices

- **New construction permits are not meeting demand.**
  California has underbuilt for years. Estimates from Beacon Economics put the backlog at about 2.3 million housing units in 2017. Just to keep pace with its growing population, California needs an average of 180,000 new homes every year, according to state housing officials. However, today the statewide numbers are moving in the wrong direction. Only 104,000 residential permits were issued in 2018, and about 95,000 are projected for 2019.

- **Vacancy rates are low and household sizes are high—especially for renters.**
  In 2018, California's 4.0 percent vacancy rate for renters was 2.1 percentage points lower than the nationwide rate and the third lowest in the nation. Meanwhile, California's homeowner vacancy rate was 1.2 percent, compared with 1.5 percent nationwide. California's rate of overcrowding—the share of housing units with more than one resident per room—was 8.3 percent in 2018, well above the national rate of 3.4 percent. Overcrowding is especially high for rental units: at 13.4 percent, it is more than twice the national rate and the highest in the nation.

- **Homeownership rates remain low.**
  In 2018, 54.8 percent of California housing units were owner occupied—10.2 percentage points lower than the rate in the rest of the nation. Indeed, New York is the only state with a lower rate. Homeownership remains 3.2 percentage points below pre-recession levels; the largest decline has occurred among 35- to 44-year-olds (9 percentage points).

NEW HOME CONSTRUCTION PERMITS DIPPED IN 2019



SOURCE: US Department of Housing and Urban Development Office of Policy Development and Research, State of the Cities Data Systems (SOCDS).

NOTE: September 2001 to September 2019.

- **High land prices—as well as labor shortages—are key drivers of unaffordability.**
  According to data from the Federal Housing Finance Agency (FHFA), 16 of the 42 counties in the country with median land prices above $1 million per acre are in California. Land prices increased sharply in many California counties between 2012 and 2017: 14 California counties were among the 20 nationwide with the largest percentage increases. Increases were especially large in San Benito, San Joaquin, Merced, Contra Costa, and Sacramento Counties. Labor shortages are also a growing concern; the unemployment rate for the construction industry has reached new lows, falling from 14.9 percent in September 2012 to 2.7 percent in September 2019.

Homelessness is widespread

- **A quarter of the nation's homeless population lives in California.**
  HUD estimates homelessness by conducting a point-in-time count on a single night in January. In 2018 (the most recent statewide data), HUD estimated that about 130,000 people in California were homeless—almost a quarter of the nationwide total and double the state's share of the US population (12%). California's rate of homelessness, 33 per 10,000 residents, is the second highest in the nation. What is more, 69 percent of homeless in California are unsheltered, living on the street or in parks and other makeshift spaces; this is the highest rate in the nation.
- **Many counties saw spikes in homelessness in 2019.**
  Los Angeles County recorded nearly 59,000 homeless people in 2019. In per capita terms, however, homelessness is a bigger problem in San Francisco and Santa Cruz Counties. Between 2017 and 2019, the number of homeless increased in all of California's large urban counties except San Diego. Santa Clara, Alameda, and Contra Costa Counties saw two-year increases of more than 40 percent. It should be noted that improvements in the accuracy of homeless counts make comparisons to past years difficult.

Looking ahead

California needs short- and long-term policies that improve housing affordability and remove unnecessary barriers to increasing supply. Because state efforts must interact with local land-use and zoning policies, addressing California's housing challenges will require the sustained cooperation of state and local governments as well as developers.

It will take time, funding, innovation, and coordination to end the homelessness crisis. The 2019–20 budget's $1 billion commitment to fighting homelessness is a step in the right direction, but continued investment is needed. Addressing homelessness requires coordination between the federal, state, and local levels, as well as collaboration across sectors (housing, health, and social services). Policies that fund both housing and supportive services are crucial: getting people into homes as quickly as possible (rapid rehousing) and connecting them to health care, treatment, education, and employment services (permanent supportive housing) are proven approaches. Leveraging private sector and philanthropic resources should be a key element of any strategy moving forward.

Localities are trying a range of approaches to improve affordability and reduce homelessness. Several cities with especially severe housing challenges recently passed local bonds to fund new housing as well as assistance for low- and middle-income households and people experiencing homelessness. For example, Los Angeles voters approved a $1.2 billion bond measure in 2016 to help fund housing for homeless people. In 2018, San Francisco voters approved a tax on larger businesses to generate $250–300 million per year for homelessness prevention and services; two additional affordable housing measures were approved in 2019. Berkeley and Oakland voters have also increased or instituted new taxes to generate revenue for housing.

Solving the affordable housing crisis requires balancing local and state control. California's tight housing market reflects not only a scarcity of developable land but also an array of policy choices. Changes to zoning and other regulatory policies are needed to help reduce the cost of building housing. Traditionally, these policies have been made at the local level, but the state has recently enacted reforms—such as streamlining the development of accessory dwelling units (ADUs)—that supersede local rules and/or motivate local policy changes.

Land-use policies should incentivize more housing while meeting environmental goals. California has passed legislation that aims to lower harmful emissions by encouraging coordination of new housing development with transportation networks at the local level. Infill (new construction in built-up areas) is one way to achieve this goal, but there is a trade-off: infill development tends to be more expensive, partly due to local opposition, and usually produces fewer units than development at the edges of urbanized areas.

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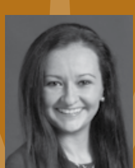

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