

Why Affordability Matters

Stuart Gabriel¹ and Gary Painter²

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¹UCLA Anderson School of Management; sgabriel@anderson.ucla.edu

²USC Price School of Public Policy; gpainter@price.usc.edu

Introduction

Recent years have witnessed widespread public concern and increased policy attention to issues of housing affordability. That concern has emanated from the marked and near ubiquitous decline in the availability of affordable housing. While numerous analyses document the generalized rise in rent burdens, few papers focus on the economic and societal implications thereof. This paper addresses the latter issue of why affordability matters. Specifically, it focuses on consequences of lack of housing affordability at both the household and metropolitan level.

In our analysis, we proceed as follows. We first define the affordability problem. Subsequently, we review literature in economics and public health to characterize the broader societal consequences of widespread deterioration in housing affordability. Finally, we speak to policy approaches pertinent to addressing the affordability challenge. Our findings suggest that elevated rent burdens are associated with a myriad of adverse household outcomes including residential crowding, long commutes, low levels of family expenditure on health care and other vital family needs, and problems of child well-being and development. At the metropolitan level, constraints on housing affordability have been associated with out-migration of households and firms to peripheral areas or beyond, increased levels of urban congestion, and deterioration in quality-of-life so as to ultimately constrain area job growth and local economic viability. Below we discuss those issues as well as related policy response.

I. The Affordability Problem

The combination of rising housing costs and muted income growth has resulted in many households devoting a large and increasing share of their income to shelter. The term “rent burden” has come to describe those households paying more than 30 percent of their monthly income on rental costs. In 2015, a full one-half of U.S. households were rent burdened (Fernald,

2015; Fernald, 2016). As would be expected, low-income and undocumented households as well as families with children disproportionately experience rent burdens (Ault, 2016; McConnell, 2013; Greulich, et al., 2004). Rent burdens have become increasingly prevalent in the wake of the Great Recession of 2007-08 with household composition and location serving as the major drivers of that phenomenon (Colburn & Allen, 2016).

In chart 1, we describe evolution of rental cost burdens among middle and lower-middle income households over the period since 1960. The computation focuses on both moderately- and severely-burdened households; e.g., those paying more than 30 and 50 percent of their income, respectively, on residential rent. The chart plots those burdens by quintiles of households (both owners and renters) sorted by pre-tax household income. We focus on rental affordability ratios among the bottom, lower middle, and middle income quintiles. As is evident in the chart, rent burdens are both highly prevalent and substantial among the bottom and lower middle income quintiles. Indeed, more than 60 and 80 percent of all households in the lower middle income and bottom quintiles experienced rental cost burdens in excess of 30 percent in 2014! Further, rental cost burdens have risen markedly in recent decades, especially among the lower middle income tier. Among that group, burdens increased from 40 percent in 2000 to over 60 percent in 2014! Substantial increase in cost-burdened households since 2000 also has been evidenced among the middle quintile.

As shown in chart 2, the increase in rental cost burdens occurred in the context of widespread metropolitan decline in the availability of rental housing. Indeed, rental vacancy rates fell sharply in virtually all major U.S. metropolitan areas over the 2010-2015 period. In all sampled areas, vacancy rates in 2015 hovered at or below 4 percent, having declined from double that level in some areas over the prior 5 years. Indeed, some cities, including New York, Los Angeles, Seattle, Detroit, San Diego, Boston, and Minneapolis, witnessed declines in rental

vacancy to roughly 2 percent! Vacancy rates in that range are far below market equilibrium levels so as to result in strong upward pressure on rents.

In many metropolitan areas, substantial numbers of households with incomes as high as \$45,000 are rent-burdened. Indeed, as shown in chart 3, a full 60 percent or more of households with incomes up to \$45,000 are cost-burdened in metropolitan areas including Washington, D.C., San Francisco, Los Angeles, New York, Miami, Boston, Seattle, and Philadelphia. For lower-income households with incomes up to \$15,000, rental cost burdens are near ubiquitous.

Finally, as shown in chart 4, rental housing cost burdens are not unique to urban areas. In fact, both housing scarcity and depressed wages give rise to an increasing share of rent burdened households in rural areas. As evidenced in the chart, rental cost burdens in excess of 30 percent are common in non-metropolitan areas of the west, the southeast, and New England. In sum, the data suggest rent burdens are both sizable and have markedly increased over recent decades for large numbers of U.S. households. Indeed, rent burdens are now pertinent to one-half of all U.S. households. Further, those concerns are not limited to a few select coastal cities, but are evidenced across a wide cross-section of both metropolitan and rural areas.

III. Consequences of Increasing Rent Burden

Hedonic Pricing theory (Rosen, 1974) suggests that rents reflect both housing services and amenities associated with a particular residential location. Amenities capitalized into rents include those that are essential to family well-being including access to jobs, quality schools, and residing in safe communities. These essential amenities are consistently the focus of families that are surveyed on the primary factors that lead to neighborhood location choice. Other

amenities that influence housing prices include environmental goods or “bads” as well as access to luxury amenities such as proximity to high end cultural institutions or restaurants.

While efficient housing markets might price housing services and amenities appropriately, resource constraints can lead to an inequitable distribution of amenities and related inferior quality-of-life outcomes for families. Further, government land-use policy and geographic contours (Saiz, 2010) may restrict housing supply and increase housing costs in the face of increasing demand without associated increases in amenities.

As households face increasing rent burdens, they are forced to make adjustments in consumption of housing services and amenities in the face of budget constraints. These choices have consequences both for individual households and for the metropolitan economy. Indeed, as discussed below, widespread affordability constraints can result in adverse externalities and ultimately damp the competitive structure and growth of a metropolitan area. In the face of high rent burdens, households may move to more affordable locations either within an existing metropolitan area or across metropolitan boundaries.

Rent Burdens and Households

As rent burdens increase, households have a number of margins of adjustment. Households can double up and live in more overcrowded conditions (Díaz McConnell, 2016; Hernández, et al., 2016). Alternatively, households can reduce spending on other goods such as food, education, health, and energy costs (Kirkpatrick & Tarasuk, 2007; Kirkpatrick & Tarasuk, 2011; Newman & Holupka, 2016). Households may also choose to move further away from job centers (Saltana, 2002) and increase commuting times. Still others may move to lower quality housing or to neighborhoods with higher crime rates or lower performing schools (Kirkpatrick & Tarasuk, 2007; Kirkpatrick & Tarasuk, 2011).

Research has consistently found negative associations on various life outcomes for households facing higher rent burdens. Much of this research has focused on the health and education outcomes of children (Lopoo & London, 2016; Mueller, & Tighe, 2007; Harkness & Newman, 2005). As indicated in chart 5, roughly one-third of cost-burdened renters are families with children. In addition, Newman and Holupka (2015) find an inverted U-shaped relationship between the fraction of income spent on housing costs, and both cognitive achievement and enrichment spending on children. The inflection point for this correlation occurs at roughly 30 percent—the standard designation of burden (Newman & Holupka, 2015; Newman & Holupka, 2016). Further, housing cost burden has been associated with declines in mental health, and cost-related health-care and prescription non-adherence among adults (Mason, et al., 2013; Pollack, Griffin, & Lynch 2010). As would be expected, rent-burdened households have substantially limited financial capacity for other vital needs, notably including food, transportation, healthcare, and retirement savings (see chart 6).

Finally, a robust literature testing the spatial mismatch hypothesis (Kain, 1992, summarizes much of the early literature) demonstrates how proximity to jobs strengthens labor force attachment and wages. Gabriel and Rosenthal (1996) test whether lower rents provide compensating differentials for these inferior labor market outcomes, but find that lower rents only provide about a 30% compensating differential.

Rent Burden and Metropolitan level impacts

The effects of housing affordability and rent burden on metropolitan-level indicators have become widely discussed in the policy field, yet remain relatively understudied because of significant identification issues in research designs. Empirical work does suggest high housing costs have served as a driver in the separation between workers' employment and residential locations, which has been correlated to increases in travel time and congestion (Cervero, 1989;

Cervero, 1996; Saltana, 2002). Other work suggests that having more equitable and inclusive housing stock is believed to create greater diversity, while reduced income inequality has been associated with stronger economic growth and a reduced impact from recessions (Turner, 2009; Abiad, et al., 2015; Benner & Pastor, 2015). However, additional work is needed to determine the efficacy of programs that might support additional affordable housing and workforce housing near job centers before conclusions can be drawn concerning region wide impact of the growing numbers of households facing rent burdens.

IV. Mitigating Adverse Consequences of High Rent Burdens

As a core strategy, policymakers in high housing cost areas should address deleterious effects of elevated rent burdens through increased housing access and supply. In many rent burdened areas, the scarcity and high costs of developable land make affordable housing development less viable to private developers. In those locales, officials can enhance the economic viability of such development via an easing of regulatory constraints notably including restrictions on housing density. Further, densified housing development can be directed to areas proximate to rapid transit, so as to limit adverse spillover effects on commutes. However, in built-out areas, remaining developable land often comes with exposure to adverse environmental amenities. Indeed, per literature cited above, there exists substantial health risks associated with siting of affordable housing within close proximity to freeways or other noxious environmental sites.

As discussed above, market forces in high land cost areas push affordable housing development to distant outlying areas. The lower peripheral land rents enable private development of affordable housing; however, those same low land rents reflect lack of access to employment opportunities and to other important amenities. Here regional policies, notably including investment in rapid transit, can lower the time and pecuniary costs of commutes while

expanding access of burdened households to reduced rent burdens. As above, planners can encourage development of affordable units in outlying areas in proximity to transit lines. Also, access to housing in distant lower-rent areas can diminish crowding. Further, in an effort to enhance educational opportunity and child outcomes in outlying, low amenity areas, state educational authorities can seek to distribute public school resources across districts in a manner that diminishes the role of local income and wealth in determination of local school quality. State and local authorities should similarly seek to ensure adequacy of environmental and recreational quality across higher- and lower-rent burden areas so as to address public health and welfare concerns described above.

At the metropolitan area level, numerous mechanisms are commonly employed to address scarcity of affordable housing and related adverse implications for job creation and retention, economic base, and competitiveness of the urban area. Per above, among the most straightforward of devices is the easing of land-use regulatory constraint so as to allow for more densified housing development. Related measures include inclusionary zoning for affordable housing development. Those efforts are often controversial among resident populations concerned about adverse externalities in the form of congestion and neighborhood quality-of-life. Accordingly, measures promoting densification and inclusionary zoning require parallel investment in transportation infrastructure to mitigate congestion impacts even as population density increases. Other well-established efforts include targeted provision of affordable housing for critical workforce, including police, fire, teachers, health professionals, and the like. While such efforts often do not address overarching affordability challenges, they do aim to preserve critical workforce consistent with maintenance of required services. Finally, cities confront abundant challenges in preservation of existing affordable housing stock associated with HUD Section 8 and like programs.

Conclusion

Recent years have witnessed a marked increase in rent-burdened households. Excessive rent burdens have become relevant even among middle tier households and across both urban and rural areas. Indeed, research suggests that a full one-half of U.S. households pay more than 30 percent of their monthly income in rent.

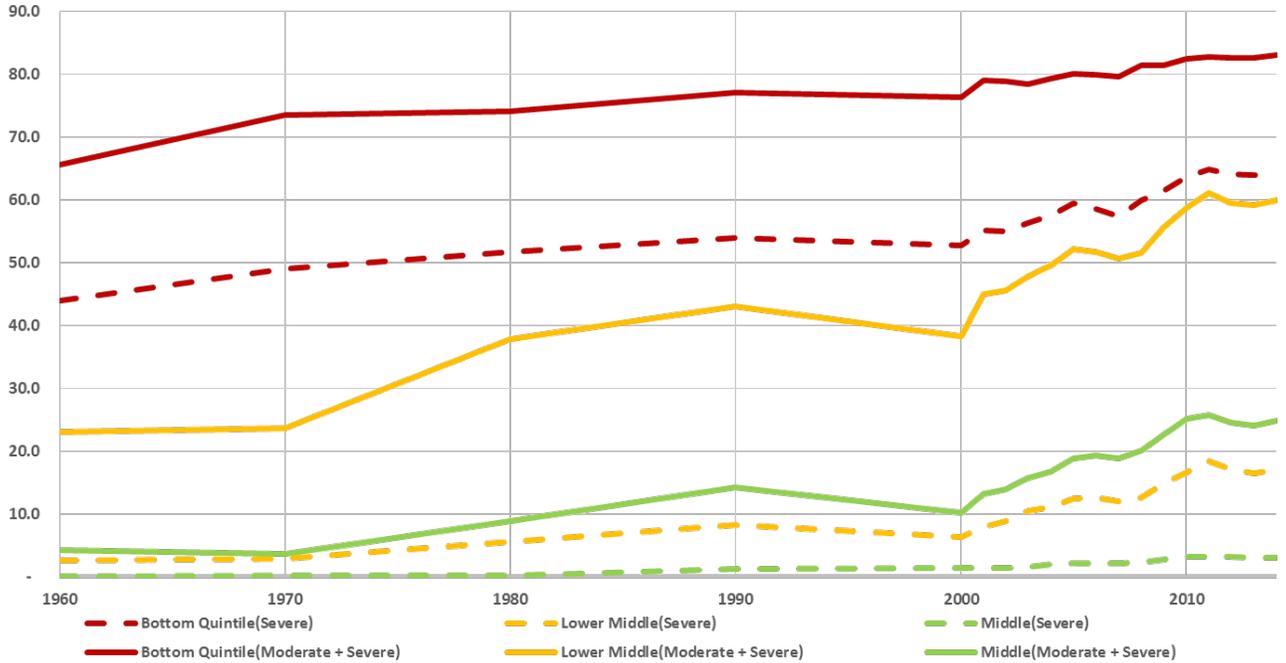
Factors driving affordability challenges vary across time and place. In many metropolitan areas, inadequacy of affordable housing stock lies at the core of the issue, owing in part to scarcity and pricing of developable land and regulatory constraints pertaining thereto. Those areas are often characterized by high levels of congestion and related problems of work access. Elsewhere, including many non-metropolitan areas, stagnation of local economies, job opportunities, and incomes have resulted in upward movement in the rent-to-income ratio. As discussed above, the appropriate response to the lack of affordable rental stock in metro areas focuses both on creation of new urban supply and enhancement of transportation infrastructure so as to access supply in peripheral and more affordable areas. In non-metropolitan areas, core solutions focus on economic development and income creation. Both areas also benefit from demand-side subsidies in the form of vouchers and the like. Regardless, local policy can and should address consequential issues of school and environmental quality, exposure to violence, access to jobs, and other adverse attributes often prevalent in low-affordability neighborhoods.

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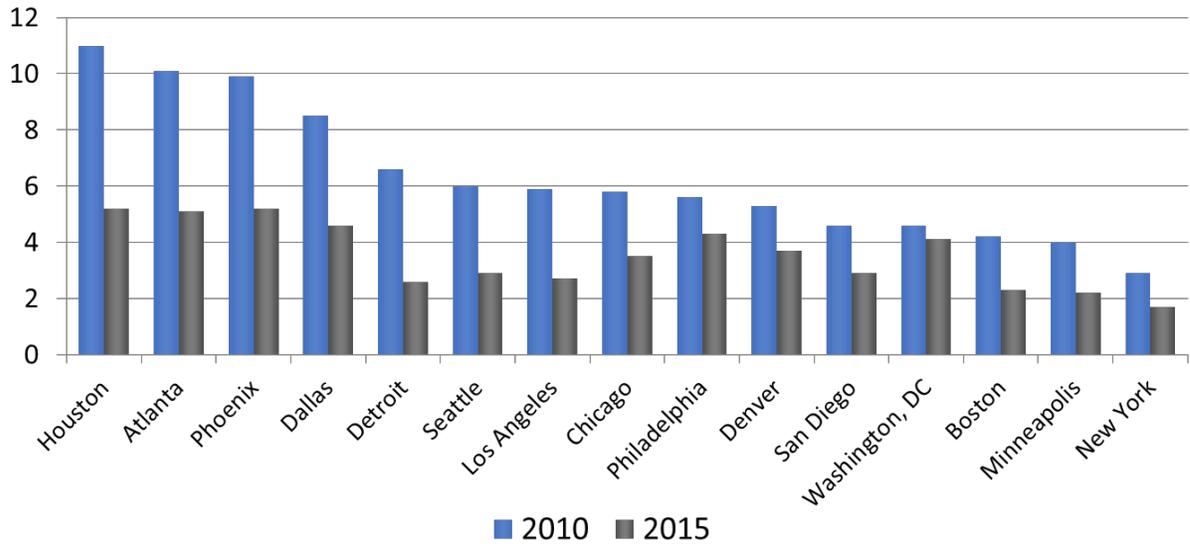
Chart 1: Renter Housing Cost Burdens by Household Income Quintiles: 1960-2014



Notes: Moderately (severely) cost-burdened households pay more than 30% and up to 50% (more than 50%) of income for housing. Households with zero or negative income are assumed to be severely burdened, while households paying no cash rent are assumed to be without burdens. Household income quintiles are equal fifths of all households (both owners and renters) sorted by pre-tax household income.

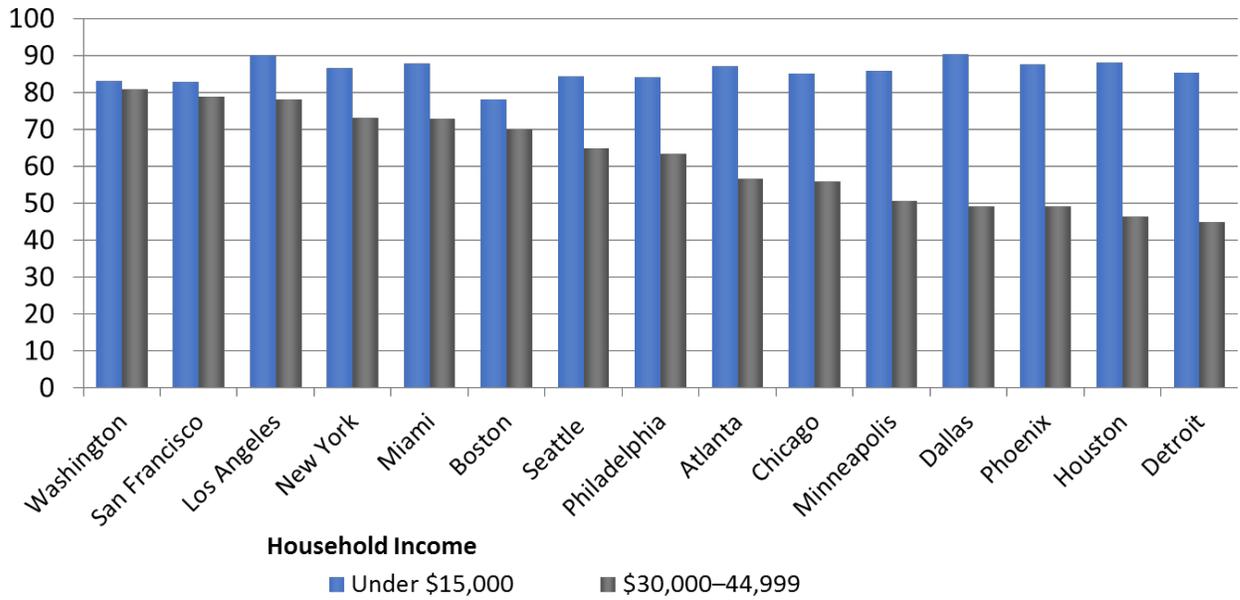
Sources: JCHS tabulations 1960-2000 Decennial Censuses and 2001-4 American Community Surveys via Steven Ruggles, J. Trent Alexander, Katie Genadek, Ronald Goeken, Matthew B. Schroeder, and Matthew Sobek. Integrated Public Use

Chart 2: Rental Vacancy Rates (Percent)



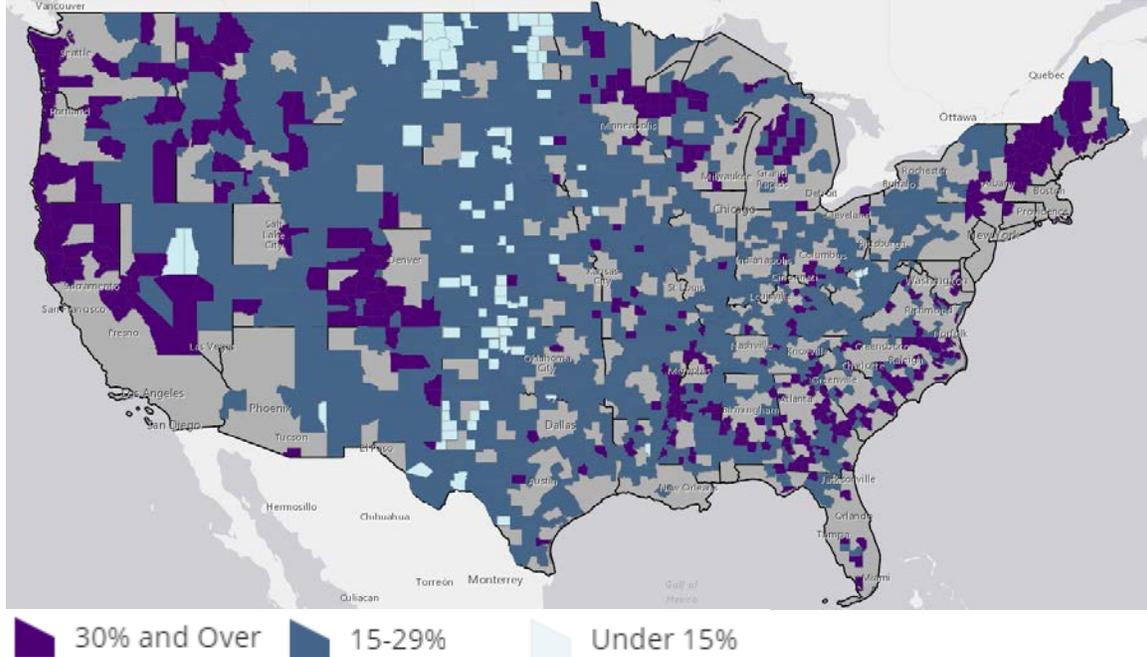
Notes: Estimates are based on a sample of apartments in investment-grade properties. Data for 2010 are from the fourth quarter. Data from 2015 are as of the third quarter.
Source: JCHS tabulations of MPF Research data.

Chart 3: Share of Renters with Cost Burdens (Percent)



Notes: Cost-burdened households pay more than 30% of income for housing. Households with zero or negative income are assumed to have cost burdens, while households paying no cash rent are assumed to be without burdens.
Source: JCHS tabulations of US Census Bureau, 2014 American Community Survey.

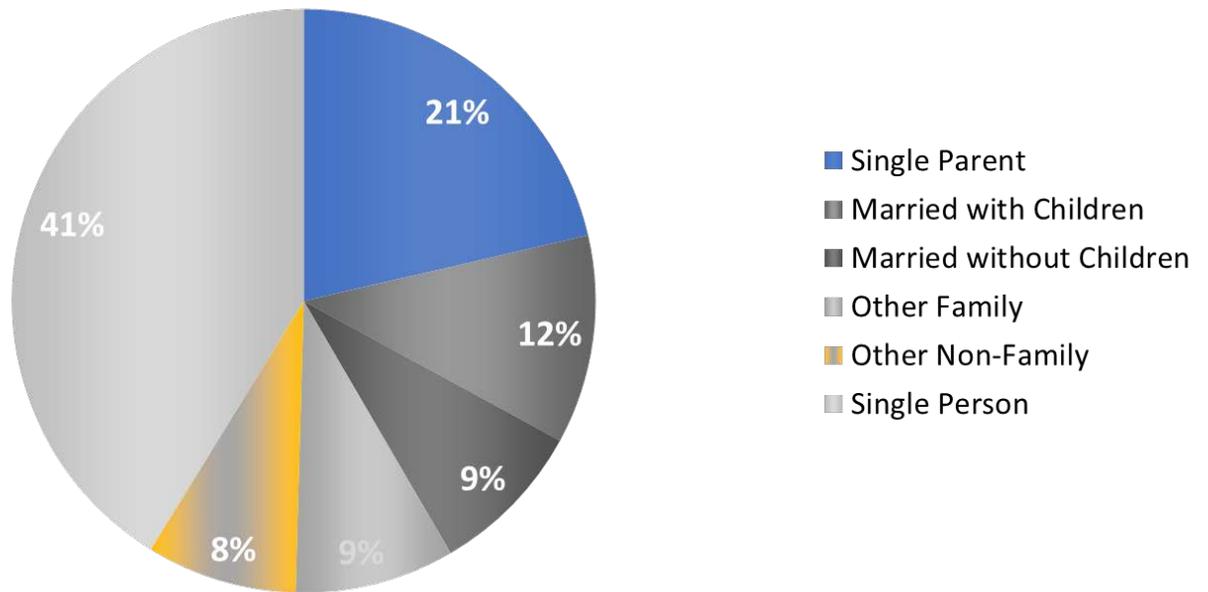
Chart 4: Share of Population that is cost burdened (owners and renters) in Non Metropolitan Areas



Notes: The map shows the share of households in non-metropolitan cities that are housing cost burdened in 2014. Households spending 30% or more of their income on housing are considered cost-burdened.

Source: Sonali Mathur, JCHS tabulations of Decennial Census and American Community Survey

Chart 5: Share of Households with Cost Burden by Family Type



Notes: Cost-burdened households pay more than 30% of income for housing. Households with zero or negative income are assumed to have severe burdens, while households paying no cash rent are assumed to be without burdens.

Source: JCHS tabulations of US Census Bureau, 2014 American Community Survey.