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## The Economic Case for Housing First

Athullya Biju Gopi

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# Bard

# **The Economic Case for Housing First**

Thesis Submitted to Levy Economics Institute of Bard College

by Athullya Biju Gopi

Annandale-on Hudson, New York May 2016

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## ABSTRACT

The federal government's entry into regulating the US housing sector began with reforms initiated during the New Deal. Given the effects of the Great Depression, the New Deal was the perfect opportunity to implement housing policies that would have ensured a more equitable distribution of housing to all households, especially those which are on the lower end of the income distribution. However, as we shall see, federal housing policy has historically followed a path that focuses purely on demand-side measures. This is not by accident; the housing sector has long been seen as a macro-stabilizer that can be used to stimulate long-term growth in the economy through capital formation and employment created by the construction sector, specifically the residential construction sector. While demand-side measures are a Keynesian prescription for full employment, the lack of counter-balancing supply-side measures prevents the housing sector from achieving an equilibrium between supply and demand in both the short and long term, meaning that effective demand is never fully met. The reason for this is primarily the way in which the housing market functions; supply is relatively price inelastic compared to demand in the short run and more elastic overall in the long run. Supply is also restricted by external factors such as land use regulation. By imposing demand-side measures in a supply-restricted market, the eventual rise in prices will tend to price out households on the lower end of the income spectrum. What results is both imminent homelessness and eventual homelessness as a result of economic rather than noneconomic conditions, which do not have supportive assistance on the homelessness policy side. This paper concludes with a proposal on how the gaps in housing policy and homelessness policy can be remedied through an increase in public housing stock combined with the Housing First<sup>1</sup> approach; an approach that does not involve means testing and extends access to housing without the fulfillment of any prerequisite conditions.

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<sup>1</sup> The "Housing First" model is a homelessness relief program that is designed to serve the immediate housing needs of the homeless by providing "immediate access to permanent supportive housing to individuals who are homeless and who have mental health and addiction problems" (Pathways Housing First 2018)

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## **I. INTRODUCTION**

Homelessness in the United States is a systemic national socioeconomic problem. Although it is now widely accepted as a highly relevant topic of social research, its importance was not highlighted until the 80s and 90s when it became more evident that homelessness was not only being caused by social factors but more so too by economic ones. Homelessness resulting from economic factors, such as the lack of adequate employment at a living wage or the lack of affordable housing, manifests more amongst low-income, poor, and extremely poor households.

However in spite of this growing phenomenon across the United States, the federal policy response has only been sufficient enough to offer a palliative cure for this chronic ailment; focusing on welfare schemes such as rental assistance and housing vouchers to induce the affordability of private housing among low-income households rather than offering more robust fiscal policies such as more efficient federal spending on the expansion of the national stock of public housing needed to meet the effective demand for housing. The inadequate level of affordable housing is often cited within non-profit and academic research literature as being the main source of homelessness and indeed there is reason to believe so in a national housing market where the supply of housing stock is dominated by the private sector that favors homeownership over renting. The high price-elastic demand and the relatively price-inelastic supply of the housing stock together lead to an asymmetric national housing market that effectively remains in disequilibrium in the long run.

This thesis first aims to show that this asymmetry is, to a large extent, precipitated by the overrepresentation of homeownership as the ultimate objective of key federal housing policies such as the National Housing Act of 1934, established under the New Deal during the Great Depression, and how such legislation has shaped the asymmetrical housing market by establishing itself on Keynesian-style demand-side principles with no counterbalance on supply-side fiscal measures.

The second aim is to show that the housing market disequilibrium, which is exacerbated by the presence of specific demand shocks, predisposes a larger proportion of moderate to low-income households on the verge of homelessness to become homeless, especially when there is growing

evidence of a decline in investment by both the public and private sector in affordable housing. These households which are on the verge of homelessness, also known as the “near” or imminently homeless, are a subset within the homeless community who are forced to ‘double-up’ in temporary places of accommodation until they can afford private and more permanent housing options. What makes their lack of access to housing a more pressing matter and an area of focus in this thesis is the fact that the imminently homeless have little or no access to the federal welfare and support programs that the physically homeless do, simply because there are no protective structures or policies in place to monitor and preemptively prevent those at risk from entering a state of homelessness. Thus when faced with a demand-shock such as a spike in rents or a decline in incomes, their level of affordability for housing weakens to the point that it causes them to shift to a state of temporary homelessness, thereby necessitating a higher and most likely inefficient level of spending on homelessness programs.

The third and final aim of this thesis is to put forward a theoretical foundation for future remedial measures aimed at mitigating the effects of ‘near’ homelessness. The proposed framework would follow the Housing First model, whereby more public housing units would be distributed to those who are at risk of being recurrently made transiently homeless. The success of this approach is theoretically based on the notion that the expansion of the housing stock would mitigate the deficiency of the housing market on the supply side while generating affordable housing for those who need more dependable sources of shelter when they are at risk of being displaced.

## **II. LITERATURE REVIEW**

### **Federal Housing Policy: Origin and Brief Overview of its Evolution**

The history of federal housing policy in the United States indicates that prior to the 1930s when the Great Depression brought about large-scale sweeping changes through the ‘New Deal,’ there was no significant participation by the federal government in the housing sector. However when we observe the set of federal housing policies in effect most of them follow a common theme; to singularly aid the expansion of homeownership. There is a dominance of the demand-side approach over federal policies, which govern the current-day housing sector that can find their

origins rooted in federal housing policy reforms established under the New Deal. The series of federal regulatory changes in housing policy that would form the basis for how the private housing sector functions today, began with the National Housing Act of 1934, which was based on short term pump-priming demand side theory, seen at the time by New Deal policy makers as the need of the hour. Much of the related literature surrounding New Deal- era housing policy changes indicate that they effectively converted housing real estate from a consumption good, whose acquisition was dependent on individual preferences, to a widely demanded investment good through policies facilitating homeownership by reducing the uncertainty of mortgage lending institutions and increasing their liquidity to finance more spending on owner-occupied housing (Kollmann and Fishback 2011; Gordon 2005; Carrozzo 2008; Nier 1999).

The advent of legislation such as the National Housing Act of 1934, as well as other federal policies undertaken in the housing sector following the New Deal, worked on actively promoting homeownership and supporting its spread into suburban rather than urban areas where housing investment was more easily financed by private lending institutions (Gordon 2005; Carrozzo 2008; Nier 1999). The reviewed literature, which spans a variety of subject categories other than macroeconomics, including sociology, law, and urban theory, collectively indicate that this new and unprecedented federal bias towards home-ownership has resulted in a rising level of inadequacy and under-development in the stock of housing, especially public housing. Additionally the modes of fiscal support offered to moderate to low-income households are not sufficient enough to ensure that all those who require affordable and adequate housing receive it (Dolbeare 1992; Landis and McClure 2010; von Hoffman 1996; Wood 1934; Shlay 2006 and Mills 1987)

The contributions by Gordon (2005), Carrozzo (2008) and Nier (1999) outline the history of the National Housing Act of 1934 and some of the preceding legislation used to describe how it came into existence. Wheelock's (2008) paper provides additional descriptive detail to the structural aspects of the Act, to better outline how it worked. Carliner's (1998) paper provides key insights into the three areas into which federal policy has expanded following its landmark entry into housing sector regulation. The emphasis on tax reforms that spur homeownership is a topic that adds weight to the argument that there is strong bias in federal policy toward homeownership and this is supported by the works of both Carliner (1998) and Poterba (1994).



Furthermore the works of Schwartz (2006), Goodman and Mayer (2018), Shlay (2006), Hoffman (1996) and Lang and Sohmer (2000) all contribute to the conclusion that towards the 80s and 90s the primary remedial measure adopted to improve the distribution of affordable housing for low-income and poor households was merely the promotion of a higher level of affordability of housing by such groups, extending fiscal benefits to the suppliers of low-income housing and further extending government support to lending institutions to enable them to lend more freely to moderate and low-income households. The stock of public housing that had been in existence since the early 1900s has not been replaced at the rate that it has been retired and the authors propose that this is reducing the access to affordable housing by low-income households.

### **Macro Theory and Macrodynamics of the Housing Sector**

The related academic literature of the macroeconomics underlying the private housing market points out that there is a general asymmetry between demand and supply in the national housing market in the United States (Goodman 2005; Riddel 2004; Glaeser and Gyourko 2005). The imbalance between supply and demand for housing is a function of both the prices and quantity of housing in the private market; in the short-run achievement of housing market equilibrium is inhibited due to the price-based rigidity of the supply curve while in the long run it is postulated that equilibrium is eventually achieved between house prices and macroeconomic variables (White and Taltavull de La Paz 2015). The general consensus is that the long-run equilibrium in the housing market is achieved only if the supply curve gains more flexibility in the long run.

With a relatively inflexible long run supply and a more volatile short-run demand, it is almost always likely that in the short run restrictions in supply will force some proportion of low-income families and individuals into homelessness, especially when the subsidies or rental assistance they receive at the federal or state level is not sufficient to meet market norms (The Institute for Children, Poverty and Homelessness [ICPH] 2015). It is therefore understood from the existing literature and research that, as a result, the effective national demand for housing may never be met by the requisite supply needed to bring the private housing market to a true long-run equilibrium that is indicative of full provision.

Thus, a section of society that needs to consume housing as shelter and not as a consumer commodity is always left unable to do so because they are ‘priced out’ of the private housing market by their inability to afford the prevalent market prices for housing.

This pricing out mechanism is a function of various macroeconomic factors, including a rise in unemployment leading to income shocks and an inadequate supply of affordable private housing owing to rental shocks, and is more prevalent in central urban areas. It is interesting to note that O’Flaherty, in his April 2009 paper, points out that while rental shocks act as a strong precipitator for homelessness, income shocks have a stronger impact on it amongst the poor (O’Flaherty 2009). As this thesis will go on to present, addressing the lack of affordable housing as a first step could potentially reduce the homelessness of individuals and families that are increasingly being excluded from accessing housing in the private housing market (United States Interagency Council on Homelessness 2017; [ICPH] 2015; Goodman 2005).

Policies that allocate federal funding for housing attempt only to increase the affordability of private housing for low income or extremely low income groups. However these measures do not mitigate the inefficiencies of an imperfect housing market and do so even less if the support being offered is constantly subject to fluctuation ([ICPH] 2015; Landis and McClure 2010; Dolbeare 1992). Even with the obvious importance that is exhibited in the literature on macroeconomy and housing and its potential impact on homelessness there is still a gap in the macroeconomic research that relates macroeconomic theory to housing market research (Leung 2004).

The focus of the federal government on targeting the ‘clearing’ of housing demand through the private sector is based on the inherent understanding that housing and especially investment in housing real estate has the capacity to influence the direction of the national economy; this influence can serve as an especially important tool during times of financial crisis. The papers by Abramovitz (1964) and Leamer (2007) refer to the operation of the housing sector over the long cycle and how this makes housing an important macro stabilizer. This fact is perhaps the source of the focus of federal policy on homeownership and forms an important part of the discussion concerning the change in housing policy approach that needs to be adopted to improve the provision of affordable housing.

The use of policy measures that target the affordability of housing is aimed at enabling households to be better predisposed to accommodate price fluctuations in the housing market. However the literature examined cites several external factors that impact short run housing demand and supply that are not price related. Mishkin (2008), Riddell (2004), Green, Malpezzi and Mayo (2005), Malpezzi and Vandell (2002) and Leamer (2007) all highlight how downwardly inflexible housing prices and rising construction costs in combination with other non-price related factors reinforce the imbalance between supply and demand for housing, further necessitating direct intervention by the federal government to bridge the resulting short-run supply gap.

The ‘affordability gap,’ as explained by Quigley and Raphael (1994), is not fully mitigated by the federal government’s existing set of affordability enhancing policies. The latter is evident from the works of Fischer and Sard (2017), Malpezzi and Vandell (2002) and O’ Flaherty (2011). The use of low income Housing Tax Credits to boost private investment in affordable housing has little impact on expanding housing stock, while government expenditures on rental assistance programs are often insufficient to meet the needs of low-income households, adding to their rental burden as housing prices and rents increase. In addition, the declining stock of public housing puts an added strain on the supply of affordable housing. The literature indicates that even with the insufficient level of spending on rental assistance programs, the federal government is reluctant to enhance or even restore its inventory of public housing stock to support the growing need for affordable housing.

The literature reviewed thus far implies that government policy concerning housing and its distribution has lost sight of the dual nature of housing demand; it is consumed both for its necessity<sup>2</sup> as a dependable and stable form of shelter as well as for its use as an investment asset that serves as an additional source of wealth for most households that buy a home. For those who consume it solely as a dependable and stable form of shelter, there are not enough protective measures to ensure that they have access to adequate housing or support when the affordability gap widens enough to render them homeless.

The works of Dolbeare (1992), Elliot and Krivo (1991), O' Flaherty (2009) collectively serve to present whom the affordability gap makes most susceptible to homelessness, also known as the imminently homeless as described earlier. Examining the existing methodologies used by the Department of Housing and Urban Development (HUD) to measure and monitor homelessness reveals a gap in the development of methods to track these imminently homeless, even though the awareness of their existence is documented in an ad-hoc survey conducted in 2013 by HUD. Collinson, Ellen and Ludwig (2015) further emphasize how federal housing policy initiatives directed at bridging the affordability gap fail to do so. Benjaminsen and Andrade (2015) and Rolnik (2013) highlight that the liberal welfare system of the United States and the neoliberally inclined facilitation of the financialization of housing in the United States are indicative of a lack of political exigency in resolutely addressing the inadequacy of affordable housing.

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<sup>2</sup> A necessity good can be considered to be one that possesses a price elasticity of demand that is relatively inelastic, meaning that when its prices rise the quantity consumed declines very little in comparison. On the contrary a luxury good is one whose consumption is more dispensable and much more elastic; the quantities consumed drop sharply with small increases in price (Kemp 1998, 592). In this regard housing could be viewed as a necessity and a luxury. The transition from one to other is dependent on the purpose for which a form of housing is consumed. Owner-occupied housing tends to espouse a sort of 'luxury' good in that if user costs rise too high, there is always the option of 'trading down' (Carliner 1998, 302) to a smaller unit or renting

Any possible solution to the housing inadequacy problem would have to follow a path that ensures that access to adequate housing is a human right that must be upheld for all. This would entail viewing housing as more than just an investment vehicle or as a macro-stabilizer, but as a necessity. A possible framework for future remedial policy measures that uphold housing as a human right lies within the Housing First model, which as described by Atherton and Nicholls (2008), is already in use within the United States to counter homelessness resulting from non-economic factors. The Housing First model would have to be coupled with an expansion of the public housing stock to successfully accommodate the model's implementation.

### **III. THE NEW DEAL AND HOUSING POLICY**

The pathway to identifying gaps in the provisioning of adequate and affordable housing to low and moderate income households (especially those at risk of being temporarily displaced into homelessness by income or rent shocks) begins by understanding how the modern-day functioning of the US housing sector came into being. Much of how the housing sector functions today in relation to the supply of and demand for either owner-occupied or rental housing depends on the framework of federal policies that have come to govern them. The foundation for this framework was originally laid through the landmark policy changes introduced by the Roosevelt administration under the New Deal; the need of the hour during the Great Depression was to promote employment creation and the rescue of a fast sinking financial sector. Prior to the New Deal the federal government had little involvement in the housing sector. When the Great Depression began, federal intervention was necessary to stem the widespread level of foreclosures in the agricultural mortgage sector and to help the economic recovery gain momentum by supporting the housing sector and thus generate employment and investment in the private sector. However as we shall see in this chapter, the approach that has consistently been used by the federal government concerning housing policy has been one that is almost entirely 'hands-off' — attempting to achieve the growth rate required to bring the economy out of a recession by stimulating the private housing sector through the mortgage lending market, while extending as little direct federal intervention as necessary, to ensure that the condition of fiscal conservatism is not compromised. This meant minimizing direct federal spending, emphasizing benefits created by tax deductions and subsidies that boost the supply of

and demand for owner-occupied housing. The objective was to maximize the level of investment in residential construction (primarily of owner occupied units but also later on, as we shall see below, of low-income rental housing) consistent with macro stability. In a subsequent chapter we will see how the housing sector has regularly been referred to as a source of macro stability and that this sourcing is more prevalent in times of economic crisis (either housing related or otherwise).

However, this chapter goes on to describe further some of the foundational policies described above and how they have placed the focus solely on promoting homeownership. Federal housing policy to ensure that every American has the right to access a decent home has therefore only ever concentrated on achieving this goal through homeownership without attempting to understand whether homeownership is the best approach to securing dependable and medium to long term shelter for households across all income groups, let alone determining whether it is the most appropriate wealth accumulation strategy for all income groups. We will examine the first measure of the Roosevelt administration: the National Housing Act of 1934 and how it changed the focus of homeownership in the postwar era. This chapter will also examine the relation of fiscal policy objectives to housing, such as tax reforms and subsidy programs further targeting the promotion of homeownership and its extension to ownership for low-income households. The chapter concludes by briefly contrasting home-ownership-oriented federal policies with other programs, such as federal rental assistance subsidies and public housing, to highlight the bias towards homeownership, and assessing whether this is the best approach to provide sustainable housing opportunities to low and moderate income households in the long run.

### **The Great Depression and The New Deal: The First Federal Housing Policies**

Prior to 1934 and the efforts to counter the Great Depression, housing was not part of the federal government's policy agenda; during that time period the construction, finance and the purchase of residential real estate were purely private decisions. The federal government exercised only a minimal level of intervention in housing-related regulations, restricting its role to the management of slum areas in large cities toward the end of 19 century, directing government credit towards agricultural lending, and to the construction of housing for war workers during World War I (Nier 1999, 619 and Gotham 2000, 305). Government policy was to allow the

market to function ‘freely’ under a liberal laissez-faire approach to meet the collective housing needs of the national economy.

The onset of the Great Depression of 1929 brought a drastic turnaround to the federal government’s approach toward housing policy in the United States. In the late 1920s and early 30s the US economy was faced with a mortgage crisis on an unprecedented scale and level. During World War I, construction of new single family and multifamily housing units was temporarily interrupted, but began to pick up pace rapidly in the late 20s to reach an all-time 30 year high by 1927, going from just under 200,000 new single-family starts valued at close to \$2 Billion to around 600,000 new single family starts valued at 5 Bn USD during that five to six year period (Wheelock 2008, 135).

The boom in housing construction during this period was naturally accompanied by an increase in the demand for short-term mortgages (Carrozzo 2008, 7). However the structure of short-term mortgages prevalent at the time varied significantly from the mortgage structures we are familiar with today. The majority of short term mortgages were structured on a repayment horizon of five to ten years. Most housing mortgages at the time were structured in a way that only necessitated the regular payment of interest at annual rates of not less than 8 percent, with the entire value of the principle due as a final ‘balloon’ payment upon maturity of the loan. Most homeowners, unable to afford the large one time repayment of principal due upon maturity, would have to default or attempt to refinance the same loan for another five to ten year period upon maturity (Carrozzo 2008, 6).

Thus, as the stock of short-term mortgages increased, so did the need to ‘roll-over’ mortgage debt. However the rapid increase in house prices led to a construction boom, as lenders got caught up in the euphoria of a bullish housing market. Mortgage lenders believed they could afford the risks associated with the increased need to roll over because the value of the underlying collateral was appreciating significantly and because the stock market provided easy financing for new construction. Eventually, the growth in housing investment far exceeded its real demand and signaled the beginning of a highly (and dangerously) speculative period in the housing market. To curb the widespread level of speculative activity, especially in the stock market, the Federal Reserve began to adopt tighter monetary policy in 1928 by raising interest

rates, putting a squeeze on housing investment (Wheelock 2008, 135). The decline in investment in housing construction precipitated a drop in house prices, with the rate of this decline increasing rapidly as the Depression began to set in; between 1928 and 1933 residential property construction declined by 95 percent and home-repair expenditures dropped by 90 percent (Nier 1999, 620).

The continued roll over of outstanding debt caused outstanding home mortgage debt to increase throughout the 1920s and into the 30s, even after the decline and leveling-off of house prices. While the nominal value of mortgage debt peaked in 1930 and subsequently declined, “deflation caused the real value of outstanding mortgage debt to continue to rise until 1932” (Wheelock 2008, 137), greatly increasing the burden of outstanding mortgage debt during the contraction phase of the Depression (Wheelock 2008, 135). This rising debt burden and the declining value of their collateral security led lenders to hold back on both the creation of new mortgages and the refinancing of existing ones (Carrozzo 2008, 7).

The drastic rise in unemployment also spurred a sudden rise in the public’s demand for immediate liquidity leading to mass withdrawals of savings deposits. This deposit drain imposed a liquidity crunch upon banks heavily invested in mortgages that could no longer be repaid as they became due, which when combined with the reduction in mortgage refinancing, created an acute shortage of funds in the mortgage lending market (Carrozzo 2008, 6).

The Home Owners Loan Act of 1933 represents the immediate federal policy response to the collapsing mortgage system and housing market of the Great Depression and forms the basis for the National Housing Act of 1934, the federal housing policy that will subsequently be examined to show how owner-occupied housing became the objective of future federal housing policies and programs. A quick overview of the Home Owners Loan Act (HOLA) and the Home Owners Loan Corporation (HOLC) that was established under it will therefore offer a more in-depth understanding of the structure of the National Housing Act of 1934.

The Home Owner’s Loan Act, first proposed by the Roosevelt administration on April the 13 1933 and approved by Congress on June the 13 of the same year, was established to help provide debt relief to the owners of homes who were unable to restructure their “balloon”



mortgage loans (Carrozzo 2008, 8). The Act provided for the establishment of the Home Owners Loan Corporation, which was created as an agency of the Federal Home Loan Bank Board with an initial capitalization of \$200 Million funded by the Reconstruction Finance Corporation and authorized for a period of three years from inception to ‘purchase and refinance delinquent home mortgages’ (Wheelock 2008, 141). With the activities of the HOLC, the federal government was keen not to repeat the mistakes it had encountered in the Federal Home Loan Bank Act of 1932 (FHLB), established under the Hoover Administration. The FHLB was originally established under the mandate of providing subsidies to reduce the construction costs of housing and supporting private home building by directly originating long-term amortized mortgages at low interest rates through a system of federal home loan banks (Gotham 2000, 305). Unfortunately the initiative was founded on an extremely risk averse view of loan origination, and ultimately led to only three known loans being originated under the program (Carrozzo 2008, 9).

The HOLC eventually replaced the loan origination role under the FHLB with one that restructured qualifying balloon mortgages into self-amortizing loans, at an interest rate of not more than five percent, spread over a 15 to 30 year maturity period (Gotham 2000, 305 and Wheelock 2008, 142). The HOLC was also authorized to issue bonds up to an initial total value of \$2 Billion (later increased to \$4.75 Billion) to finance the purchase of either defaulting mortgages or mortgages that had foreclosed within the previous 24 months from the portfolios of banks that held such delinquent mortgages. The mortgages had to have a value lower than \$14,000 or 80 percent of the total appraised value and had to be issued on 1-to-4-family properties (Wheelock 2008, 141 and Carrozzo 2008, 9). Interest earned on the HOLC-issued bonds was set at a maximum of four percent, federally guaranteed and exempt from federal, state, and local taxes. The bonds had a maturity of 18 years (Carrozzo 2008, 8).

The HOLC also established a more standardized method of appraisal of properties throughout the United States, in an effort to more accurately assess the risks on mortgage loans being purchased and restructured. The appraisal system that was put in place however was a color-coded rating system that identified desirable neighborhoods where investment and appreciation of property values were more likely. These neighborhoods were predominantly White suburban areas and coded green, with the worst-off neighborhoods being completely or even partially

Black urban ones, coded red. While there is significant evidence that shows that the HOLC provided unbiased mortgage assistance to the areas most in need, the areas that were moderate to high risk as classified under the appraisal system (yellow to red respectively) and the encouragement of the appraisal system's extensive use as a model for risk assessment by private credit institutions, ultimately led to the form of lender discrimination that strongly prevailed well into the late 60s and is more commonly referred to as 'redlining' (Carrozzo 2008, 18 and Nier 1999, 623- 624).

The aspect of the HOLC's role that is most relevant to this discussion is that of assisting mortgage lenders in achieving a higher level of liquidity that ensured the continued availability of funding for future mortgages. As was discussed during the drafting of the HOLC bill, the conceptual approach towards achieving this higher level of liquidity was through the conversion of relatively illiquid long-term mortgage assets on lenders' balance sheets into 'highly marketable' HOLC issued securities that would potentially be traded by other financial institutions for cash. This source of external financing, facilitated by the HOLC, would enable private lenders to access continuously the liquidity they required to continue originating mortgage loans with only a minimal level of intervention by the federal government. While the idea of a 'highly marketable security' was proposed during the draft phase of the bill, the execution of the infrastructure needed to increase the marketability of HOLC-related securities, indeed to even generate a secondary market for them, did not arise until the implementation of the National Housing Act of 1934. To achieve the most crucial objective of stabilizing the sinking national mortgage lending market, lawmakers felt that the framework for long-term and steady amortization, as achieved through the HOLC's activities, would increase stability in mortgage lending and make them more attractive investments for financial institutions in the long run because it encouraged 'unencumbered' home ownership to borrowers of mortgage loans over a much longer repayment horizon than had previously existed (Carrozzo 2008, 12).

The hallmark of New Deal housing policy reform is the transition in views on homeownership; from one where it would be the eventual fulfillment of the distant dream of financial security, to one that homeownership can and should be part of every individual's long-term aspirations for stability and growth. Of course this transition in views would not have existed without the government's newfound interventionist approach towards the housing sector of ensuring that

there was long-term stability in homeownership and that the uncertainties of past experiences associated with it were being eliminated through federal-level policy change.

However the government was not primarily motivated by a need to ensure the housing security of the American people, but rather to prevent the fragility of financial structures experienced during the Great Depression. To strengthen the mortgage-lending market, and indirectly influence residential construction, measures had to be taken to eliminate the possibility of illiquidity as seen at the beginning of the Great Depression. Therefore, to ensure that there was a stable and growing market where mortgage lenders could obtain the financial liquidity required to continue issuing new mortgage debt, the government decided to create a secondary market that would ensure the marketability of the fledgling asset-backed securities created by the HOLC. The institutional structures, as envisaged during the inception of the HOLC and that formed the basis for this secondary market, were established through the National Housing Act of 1934.

The National Housing Act of 1934 was drafted to provide a permanent remedy to the flawed mortgage lending system; the HOLC was merely a temporary ‘band-aid’ to treat the emergency situation at hand and was not implemented with the view of being a permanent solution. While the federal government’s aim was to stimulate housing construction, it wanted to achieve this without any significant additional outlay of government spending. The drafters of the National Housing Act sought instead to direct private enterprise toward driving residential construction by providing more favorable conditions for home financing by replacing the then prevalent approach of mortgage refinancing with self-amortizing longer-term lending (Carrozzo 2008, 24). The basic framework of the National Housing Act was expanded from the existing policy framework of the HOLC, with some significant additions. The aims of the National Housing Act of 1934 can be distilled into four categories.

Firstly, it sought further to establish a stable mortgage instrument based on conditions similar to the restructuring conditions of the HOLC: amortized mortgages that could gradually be repaid from monthly incomes in full over much longer periods thereby offering continued stability in homeownership to borrowers.

Secondly, it sought to continue to increase the stability of mortgage investments for lenders through the establishment of a federal mortgage insurance program on qualifying mortgage loans issued either 1) for the purchase or improvements to existing single family units and rental projects (multifamily units) or 2) for the construction of new ones. The mortgage insurance program was to be administered by an agency specially established for this purpose, called the Federal Housing Administration (FHA). The FHA would insure mortgages that only met certain criteria such as amortization, a maximum interest rate of 5 percent and a maximum loan value of \$16,000 (Wheelock 2008). Other qualifying criteria included a maximum loan to value ratio of 80 percent, which was subsequently raised via amendments to the Act passed in 1937 to 90 percent on mortgages to new homes of a maximum value of \$5,400 in an effort to stimulate homeownership among middle- to low- income households.

Prior to the establishment of the FHA the minimum downpayment required by private lenders on new mortgages was 30 percent of the property value, thus the changes proposed in the NHA significantly improved the accessibility of housing finance (Nier 1999). The mortgage insurance program, like other insurance schemes, collected an annual premium of between 0.5 and 1 percent of the outstanding principal on the loan (Wheelock 2008). Since the premium collected would form the pool from which indemnifications would be made the costs to taxpayers would be minimal, fitting well with the Roosevelt administration's plans to keep fiscal spending associated with the policy at a minimum. The risk underwriting of loans that were to be insured however would continue to follow the racially discriminative method of property appraisal established under the HOLC.

The insurance program guaranteed that in the event of a foreclosure due to default, the foreclosing property would be transferred to the FHA and the mortgage lender would receive debentures bearing an interest of three percent and a maturity of three years beyond the mortgage maturity in exchange. The FHA would then proceed to sell the property and if the sale occurred before the maturity of the mortgage the debentures would be redeemed (Carrozzo 2008, 39). Thus, the process of indemnification under the insurance program came with the added bonus of liquidation of the underlying property asset being undertaken by a third-party government enterprise. In this way lenders would be more secure in their capacity to expand mortgage investments.

Thirdly, since the Act was being pursued to stimulate building it was formulated to alleviate the problems of large-scale unemployment that existed in building-related trades. The loans insured by the FHA also covered loans extended for the repair, expansion, and alteration of existing homes to create additional employment in building trades (Carrozzo 2008).

Lastly, but most importantly, the Act sought to completely reform the American mortgage system itself by creating liquidity to private lenders to expand mortgage lending. The National Housing Act of 1934 incorporated provisions for the creation of private ‘national mortgage associations’ which were essentially ‘private mortgage lending institutions’ that would engage in the purchase and sale of financial instruments backed by pools of these new and more ‘secure’ mortgages. These mortgage associations would then purchase insured mortgage loans outright from local lenders at a favorable price thus releasing new funds to local lenders for investment. Surprisingly however, even with the federal mandate for provisions made to facilitate their creation incorporated in the NHA, private mortgage associations did not materialize given that lenders were still skeptical about mortgage markets. Following several years of inaction the federal government, through amendments introduced in 1937 to the 1934 Housing Act, itself established a national mortgage association, named the Federal National Mortgage Association, or Fannie Mae for short, as an extension of the Reconstruction Finance Corporation.

This new entity would provide a national market for mortgages and would be able to distribute insured mortgages from areas with a surplus of funds to ones with a deficit. Furthermore, it sought to issue debt instruments against a packaged ‘pool’ of insured and secure mortgages (assets) that could be freely bought and sold on the open market to generate funds that could be used to purchase more newly issued FHA mortgage loans (Carrozzo 2008, 42-43 and Wheelock 2008, 145). This self-perpetuating mode of financing the purchase and issuance of new FHA insured mortgages satisfied the federal government’s objective of limiting expenditure and secured Congressional support for the new legislation by maintaining a balanced budget and supporting private enterprise.

The success of New Deal housing policy can be seen in the results: the number of housing starts and sales grew from 332,000 units in 1936 to 619,000 in 1941, the national mortgage foreclosure rate dropped from 250,000 nonfarm units in 1932 to 18,000 in 1951 and by the end of 1972, the FHA had assisted 11,000,000 families in purchasing new homes and another 22 Million families in making home improvements (Nier 1999, 625).

The bias toward homeownership has remained largely the basis for any subsequent housing policy reforms undertaken since the 1930s. An indication of this bias towards owner-occupied housing is the level of federal funding that is directed towards homeowners versus renters; in 2008 the federal government spent \$6 on assistance to homeowners for every dollar spent on assistance to low-income renters (Landis and McClure 2010, 320). This difference in funding is not based on the fact that the needs of owner-occupied housing may be higher than those of renters; income from homeowners' imputed rent in the same year was recorded as \$ 59,886 compared with \$28,921, but the percentage of income spent on housing-related expenses was only 20 percent for homeowners versus 30 percent for renters (Landis and McClure 2010, 343).

### **Housing Policies Following the New Deal**

Federal involvement in housing policy over the years since the 1930s has been in three main areas: the regulation of and influence over the mortgage market, tax policy associated with housing and the provision of direct subsidies to housing producers and consumers (Carliner 1998, 300). Policies and programs based on the first two approaches are used at times when it is necessary for the federal government to provide a macroeconomic stimulus to boost investment via the residential construction sector, while direct subsidies and public housing are offered as assistance to improve affordability of rental housing to low-income families and have usually taken up the least space in the set of policies targeting homeownership. The first area of federal involvement has already been covered. The rest of this chapter will cover tax and subsidy policies and the influence they have on the housing sector.

Tax subsidies in the form of deductions of home mortgage interest and property taxes from reported income are the largest form of federal assistance associated with the housing sector; federal expenditure on housing assistance was less than \$32.9 billion in 2004 whereas tax benefits including mortgage interest deductions exceeded \$100 billion in the same year

(Schwartz 2006, 5). The federal housing policy interventions, drafted during the Great Depression, did not include tax reform since the purpose of their implementation was to offer a quick remedial solution to the failing mortgage market with as little government expenditure as possible.

The importance of the tax deductions on home mortgage interest and property taxes became first apparent during the large-scale tax reforms of the Reagan era in the mid to late 1980s. The Tax Reform Act of 1986 introduced a distinction between the interest paid on home mortgages and other forms of consumer interest. The former along with property tax were retained as deductions on personal income in the Act while other nonmortgage consumer interest and some state and local taxes were removed as deductions. The 1986 Tax Reform also eliminated the enhanced provisions, introduced earlier in the 1981 Economic Recovery Act, which made investment in rental housing more lucrative. Aside from these deductions the exclusion of imputed rents of homeowners from taxable income also constitutes a considerable form of tax subsidy that implicitly supports homeownership. Imputed rents are considered as the rents that homeowners are implicitly receiving from being their own landlords. In theory this is income in kind for homeowners that should be taxed but is considered equivalent to any other noncash implicit income that is not subject to income tax, such as the value of food consumed by farmers that they have cultivated themselves (Carliner 1998, 301–2).

Other forms of tax subsidies that homeowners benefit from include: 1) a tax subsidy introduced in 1951 that enables the rollover (Carliner 1998, 302) of capital gains from the sale of one home while buying another one of equal or greater value (trading up), 2) the provision in the Revenue Act of 1964 that enabled a one-time tax exemption from capital gains on sales for owners of age 55 or older who choose to purchase a smaller home or rent instead and 3) the Tax Payer Relief Act of 1997, which replaced the roll-over of capital gains tax and the exemption of taxation on capital gains of homeowners above 55 years of up to \$125,000 with a much higher exemption threshold of \$500,000 available to homeowners of any age filing joint returns under family status. The latter both incentivized homeownership and disincentivized the decision to rent or trade down instead (Carliner 1998, 302). These policies were enacted in response to the notion that the rollover provision had led to an over investment in suburban real estate and the

simultaneous decline in development of urban areas (Carliner 1998, 302). These incentives have all had a dominant influence on driving the federal agenda of increasing homeownership.

The spectrum of federal incentives that influence investment in rental housing (and thus the supply of housing for moderate to low-income households) appears to be quite limited in comparison to that of homeownership. The two most prominent forms of tax subsidies available to investors in rental housing are tax credits for investment in low-income housing and projects that aid the rehabilitation and revitalization of historic areas and low interest mortgages subsidized through state and local governments through revenues from the issuance of mortgage revenue bonds and mortgage revenue certificates that are tax exempt (Carliner 1998, 303 and Schwartz 2006, 5).

The tax benefits accruing to home owners are a direct function of the parameters that govern each individual homeowner's 'after-tax user cost of homeownership'<sup>3</sup>, such as the nominal interest rate, the property tax rate, the depreciation rate of property and the household's marginal federal income tax rate, and is therefore easily determined. The tax benefits accruing to rental housing however are not as easily determined; tax subsidies to rental housing depend on the tax rates applicable to the "marginal rental landlord," whose tax parameters in turn determine the rental rate that prevails in the market. Depending on the characteristics assumed for the "marginal rental landlord," these tax parameters and thus the tax subsidies that accrue to them vary greatly because the tax rate differs depending on the characteristics chosen for the marginal rental landlord. This in turn impacts the user costs that the 'marginal rental landlord' faces (Poterba 1994, 246 –47).

Take, for example, the case of a marginal rental landlord assumed to be a "top-bracket individual investor"; such an investor receives the most benefit from depreciation allowances on rental property, as they are entitled to a larger deduction that reduces the taxable income,

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<sup>3</sup> User cost in this instance is assumed to be the "marginal cost of an incremental dollar of owner-occupied housing, including the forgone return on the owner's equity," where forgone return on owner's equity refers to imputed rents (Poterba 1994, 242). User cost is usually defined by the nominal interest rate, the property tax rate per dollar of property value, the household's marginal federal income tax rate, depreciation rate of the property, the expected rate of price appreciation and the real price of owner-occupied housing (Poterba 1994, 243) Riddel 2004 refers to user cost as "the after-tax inflation-adjusted cost of homeownership" (Riddel 2004, 125). Riddell identifies the user cost as a "non-linear function of interest rates, taxes and the expected rate of future house price appreciation. Quigley and Raphael (2004) also include a similar interpretation of user cost in their paper.



stimulating higher investment in rental real estate and thereby reducing the overall rent in the rental market. However if the marginal rental landlord's characteristics place him/her in a lower tax bracket these deductions are also reduced and as a result the overall rents would be pushed up as investment in rental real estate declines (Poterba 1994, 246–47). The 1981 Economic Recovery Tax Act improved tax benefits to investors of rental real estate through reforms that considerably reduced the tax lifetime on such properties and reduced marginal tax rates, however the introduction of more stringent depreciation methods in the 1986 Tax Reform Act eliminated these tax benefits, causing real rents to rise as investors in rental real estate anticipated diminishing returns on their depreciation- related tax benefits (Poterba 1994, 247).

Comparing and contrasting the various approaches that exist within the federal housing policies, it is evident that homeownership appears to be the predominant policy objective, and is used to indirectly guide the housing sector in this direction. However it appears to be a response to the need to increase investment in a sector with a dominant impact on growth and employment. As we have seen from the New Deal policy reforms, residential construction has historically been considered a part of the construction sector that is easily influenced by government policy and so it would be a logical choice when attempting to target a sector that could be the source for a countercyclical macroeconomic policy. This emphasis on residential construction as a means for macro-economic stimulation and the federal government's focused attempts to provide an unimpeded source of liquidity to private mortgage lenders seeking higher returns on their mortgage lending in secondary markets, may be in direct conflict with what housing policy should attempt to achieve, which is to provide stable, dependable and permanent sources of shelter to all those who demand it.

### **If Not Homeownership, Then What?**

What, therefore, is the recourse for those who cannot afford to own homes in an economic and policy environment that only seems to favor homeownership as a solution to accessing dependable, stable and permanent forms of shelter? The federal government's policy solution to the latter question appears in the form of housing subsidy programs that 'subsidize' home ownership to those who would otherwise be unable to afford owner-occupied housing at the prevailing market price as result of restricted growth in incomes and access to credit facilities. The most widely accepted historical explanation for this inability to access mortgage financing,

especially amongst Black and minority groups who are most likely to face housing affordability issues due to restricted incomes and access to credit, stems from the racial segregation and discriminatory lending practices that were propagated by the NHA's standardized property appraisal system. As described earlier, this system led to white suburban households gaining a significant comparative advantage over their black counterparts in accumulating wealth through homeownership, that negatively impacted financial and human capital gains amongst blacks over a thirty year period since the FHA was first established.

The end of redlining finally came with the signing of the Fair Housing Act in 1968 that mandated the extension of housing opportunities to marginalized Blacks and minorities and to improve residential integration (Nier 1999, 630). However the Fair Housing Act merely aimed to make home-ownership more affordable to those who were discriminated against in the mortgage lending market. Once again the approach adopted was to propose below-market rate mortgage programs, only this time it was to racially marginalized groups. The Act failed to make adequate housing directly more accessible to these groups and still left a gaping hole where a solution was necessary to expand swiftly the access of housing to those who had missed opportunities for income and wealth expansion over the three decades that had passed between the New Deal reforms and its implementation.

An example of direct intervention that took place around the same time as the implementation of the Fair Housing Act, that tried to improve the direct access to housing was the development of the Housing and Urban Development Act of 1968. This came following a report by President Johnson's Committee on Urban Housing (the Kaiser Committee) which stressed the urgency to increase production of housing units to provide for the baby boom generation's expanding household size and to replace the stock of substandard housing in existence from the post WWI era. The formal proposal in December of 1968 did not place much emphasis on homeownership and for a change directed federal intervention to set a goal of producing 26 Million new or renovated units over the course of the next ten years. However, in pages 3957–58 of Lyndon B. Johnson's recorded message of the Congressional Record of the second session of the 90 Congress in 1968, it mentions that this federal legislature implicitly contained a proposal to offer low-income families the ability to buy "modest homes financed and built by the private sector" (quoted in Carliner [1998, 312]) by offering higher subsidies to private mortgage lenders

which would enable them to offer more below-market-rate mortgages to poorer individuals for the purchase of newly built homes or for the improvement of existing ones.

Once again an opportunity for the federal government to disconnect the access to housing from the influence of the financial sector fell through policy cracks, even in the face of the dismal living conditions faced by up to 20 Million Americans at the time, housed in substandard housing units (Carliner 1998, 310-3 –12). Under Section 235 of the Act a first wave of government financing for the construction of 400,000 homes, specifically for low and moderate-income families, took place (Carliner 1998, 310–12). Having little or no experience in lending into the private construction sector, the government faced heavy losses when low-income families who were sold sub-standard housing at above market prices began to default on loan payments due to the excessive cost of repairs that extended their debt beyond their means of repayment. The HUD had to take over units on defaulting loans while sellers and lenders benefited, with the burden of higher subsidies transferred to the taxpayer (Carliner 1998, 310–12).

The strong focus on home-ownership becomes more evident when key federal policies began to address low-income homeownership as a key federal goal in the 1980s and 90s. The attempted elimination in the early 70s, of discriminatory lending practices that existed through red-lining paved the way for community reinvestment initiatives that were ultimately federally mandated; mortgage lenders, specifically savings and loans institutions were expected to reinvest into the communities from which they received deposits. Those that failed to do so were “disinvesting” in these communities and eventually causing their decline by essentially taking deposits from these declining communities and reinvesting them elsewhere. The advocacy for community reinvestment initiatives to gain more prominence led to the establishment of two key federal policies that attempted to address the inequality that arose from the disinvestment that was forcing more urban areas into decline: the Home Mortgage Disclosure Act of 1975 and the Community Reinvestment Act of 1977. The former necessitated that lenders should report where they extended residential lending, enabling it to be monitored to ensure that discriminatory practices leading to disinvestment were not taking place, while the latter made reinvestment a federal requirement.

Low-income homeownership was not an integral part of the approach to federally mandated community reinvestment initiatives, however towards the turn of the 20 century it began to enter in as a prominent policy goal at their inception, (Shlay 2006, 515). There were a variety of reasons that led to this shift but the one that is most relevant to this discussion is the fact that low-income homebuyers were being recognized as a subset of the demand spectrum for housing real estate that remained “untapped”. Federal housing policy structures from the New Deal promoting homeownership originally targeted the section of the American population that constituted white suburban neighborhoods. This subset became more or less saturated as evidenced by the stagnation of home ownership rates towards the late 1980s and early 90s; a new target base for residential mortgages was needed to achieve a financial market-based macroeconomic stimulus.

In 1992, the Federal Housing Enterprises Financial Safety and Soundness Act, which was established to set specific ‘performance targets’ for government-sponsored enterprises (GSEs) such as Fannie Mae, aimed to expand homeownership to a broader range of households. HUD also expanded its reach to low- and moderate-income households by setting targets on the purchase of loans made to such households in central cities. Both the Clinton and Bush administrations focused federal policy efforts on increasing homeownership overall by improving the rate of low-income homeownership (Shlay 2006, 515). In 1995, President Clinton proposed the National Homeownership Strategy with the intent of improving overall homeownership rates up to 67.5 percent. In 2003, George W. Bush signed the American Dream Downpayment Initiative to help first time homeowners secure a downpayment (Goodman and Mayer 2018).

Apart from the purpose that low- and moderate-income homeowners would serve as the new target base needed to stimulate economic growth via the housing sector, the expansion of homeownership opportunities toward such households was also based on the government’s inherent assumption that the social benefits of homeownership would be imputed to more low-income households by making them appear as ‘safer’ investment options to private mortgage lenders where they would once have been deemed too risky to extend mortgage loans to.

With hindsight it is clear that these policies were adopted without considering whether homeownership provides the best possible means to ensure low to moderate-income households' access affordable housing of acceptable quality. As seen in the example of the failure of Section 235, low-income households are less capable of facing the uncertainty of fluctuating housing user costs in the long run. The economic benefits to low-income households of homeownership depends on whether or not owning a home is a better long-term strategy for wealth accumulation than renting or investing in other financial assets. The gains of homeownership to low and moderate income households are found to be more sensitive to factors such as when such buyers enter and exit the cycle of housing prices, the number of units they are able to invest in simultaneously and how long they are able to hold their investments. Considering that these variables are not considered in the federal policy framework specifically targeting low-income homeownership, it is important to question whether or not homeownership as strongly emphasized by the federal government is the most appropriate presumption for federal housing policies, especially when income inequality has been consistently increasing over the last several decades (Shlay 2006, 519).

While promoting homeownership has been a consistent aspect of federal housing policies, the federal government to a lesser extent also provides assistance in the form of subsidies for low-income households. This is provided in three specific ways: the direct promotion of the construction and development of specific low and moderate income housing developments, assistance to renters to pay for private rental units through the voucher system; the funding of state and local authorities to develop housing through the block grant system (Schwartz 2006, 5). The Housing Act of 1949 and the accompanying title programs consolidated the efforts of the federal government to support public housing projects starting in the 1930s, especially concerning slum clearance and the aim to rehouse the majority of the American population in European-style public housing projects (von Hoffmann 1996, 424). However, similar to the controversial handling of the Section 235 program, the Title III amendment to the Act, which engaged the federal government in building 810,000 new public housing units, was eventually challenged and subjected to conditions that rendered it ineffective in achieving its original goal. On the contrary, the Title II program of the same Act, which increased the FHA's authorization of mortgage insurance, was termed more successful than the others in achieving its aim of extending homeownership (Lang and Sohmer 2000, 296).

The direct intervention in the provision of public housing by the federal government has always been met with political resistance; implementation problems associated with the public sector engaging in activities dominated by the private sector and the inability to successfully translate program initiatives into workable housing solutions for the poor have historically impeded further development of such initiatives at the federal level. The Housing Act of 1949 is even seen to have created outcomes contradicting its original aim of creating decent housing for all Americans; the urban redevelopment policies it advocated led to more units being destroyed in the name of urbanization than were eventually replaced. The Act also attempted to generate ‘visionary’ changes in public housing by constructing high-rise buildings as a source of affordable housing for the poor, leading to an increase in racial discrimination and income inequality amongst the urban poor where they became concentrated in areas dominated by such federal housing projects (von Hoffmann 1996, 424).

## **Conclusion**

The conclusion to this chapter will analyze whether the adoption of federal housing policies in the direction of homeownership can still be considered valid given the changes in the trends towards homeownership following the most recent financial crisis. Until WWII a sizeable proportion of households in the United States were renters as opposed to owners of their own home, with urban areas being more highly populated than suburban areas (Schwartz 2006, 11). Housing policies and programs prior to 1934, had not yet evolved to the federal level as they did during the Great Depression. Additionally during this time, the private construction of residential homes and commercial mortgage lending were less interlinked than they are today, while the oversight of safety and habitability standards of properties and the protection of existing property owners was mainly the remit of state and local governments (Landis and McClure 2010, 321 and Carliner 1998, 304).

Closer to the early 2000s it is very evident that this trend had been completely reversed with a marked increase in the suburban versus urban population (although urban population density is considered higher than suburban), and the total number of renters declining in comparison to the number of homeowners (Schwartz 2006, 11). These facts, as pointed out by Schwartz in the 2006 edition of his book *Housing Policy in the United States*, correctly described trends in the

housing sector; that is, until the onset of the Great Recession in 2007 when the US housing market crashed and housing prices plummeted, setting in motion a series of changes in housing consumption patterns that were quite different from what they had been in the run-up to the global financial crisis.

Subsequent trends in the private housing sector have shown a decline in the profitability of owner-occupied housing in comparison to rental housing. Figures 1, 2 and 3 at the end of this chapter reflect data on the United States between 2000 and 2016 and indicate trends in rent prices, real house prices and rent-to-price ratios (measure of profitability of owner-occupied housing), between 2006 and 2017 from the Organization for Economic Co-operation and Development (OECD) Housing Indicator for 2018 with base year in 2010. Figures 1 and 2 respectively show that there has been a larger increase in rental prices from the base year of 2010 to 2016 (16 index points) than in the real price of housing within the same period (around 14 index points). This indicates a growing demand for rental housing rather than owner-occupied housing in the United States during the period of recovery following the global financial crisis, in spite of the rebound in the housing market as seen in figure 2 indicating the trends in real prices.

This change can be explained to an extent by the continued stringency in mortgage lending; the reduction in credit on homeownership rates has caused a 7 percent decline between 2005 and 2015 that could not significantly be explained by the usual demographic argument of unfair lending practices directed toward blacks and racial minorities (Goodman and Mayer 2018). A more robust explanation for this trend is the rise in single-family rental units that have been absorbing most of the housing demand in the post-recessionary recovery period, instead of owner-occupied homes (Strochak 2017 and Sullivan 2017). In the period immediately following the recession, as foreclosure rates for single-family units began to increase, institutional investors quickly began to buy up these units for below market value rates. Given the tighter post-recession mortgage lending terms, middle-to-low-income households are beginning to shift to renting single-family units where they would have instead purchased them at the height of the property boom, just prior to the recession.

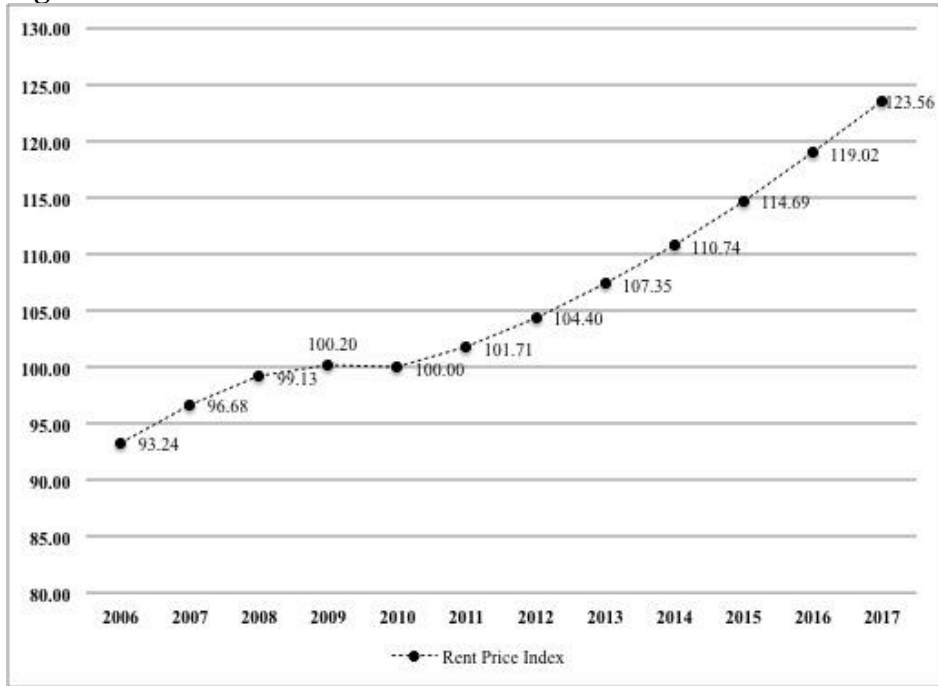
This spike in demand has even initiated a change in the home-building market, where housing firms are beginning to actively adopt a ‘build-to-rent model’ to cater to the growing demand (Sullivan 2017). While institutional investors still remain a relatively small proportion of the single-family rental market, owning around 2 percent of the estimated 15 million single-family rental units nationwide in comparison with 55 percent of the multifamily rental units, this new trend appears to be bolstered by demographic and housing-market conditions that are increasing the demand for rental units rather than homeownership (Strochak 2017)

However, in spite of the changes in investment trends that have been building up over the past decade or so in the post recessionary phase, the federal policy space concerning housing has not adapted significantly to accommodate them; this is counterintuitive considering that the last set of significant changes in housing policy were precipitated by the Great Depression, an economic meltdown of similar and greater proportions.

The housing sector in the United States is still characterized by an overdependency on the private sector and the private mortgage market, supplying the needed housing stock and financing respectively, to meet the demand for housing across the majority of the consumer income spectrum. This inadvertently leads to a worsening of the affordability of owner-occupied housing when incomes are not growing in proportion with house prices and mortgage credit is more difficult to access. The same applies to rental housing when rent-to-price ratios are comparatively low (Gallin 2004); a trend that is re-emerging following its increase during the Global Financial Crisis (see Figure 3 below). A declining stock of affordable housing in the private and public sectors further adds to the downward pressure on affordability, especially in times of demand shocks. Yet there are no signs of any significant federal housing policy changes being proposed to counter such problems in a manner that does not focus on homeownership, which under the given circumstances of the most recent recession being precipitated by inconsistencies in the primary secondary mortgage markets begs the question as to why a different federal approach based on the direct provisioning of housing is not on the horizon. The answer lies in the bias of the United States housing sector towards owner occupancy (across all income groups) as a result of the approaches adopted under federal housing policy changes beginning in the 1930s and the subsequent legislation and programs that were established to promote countercyclical macro policy.

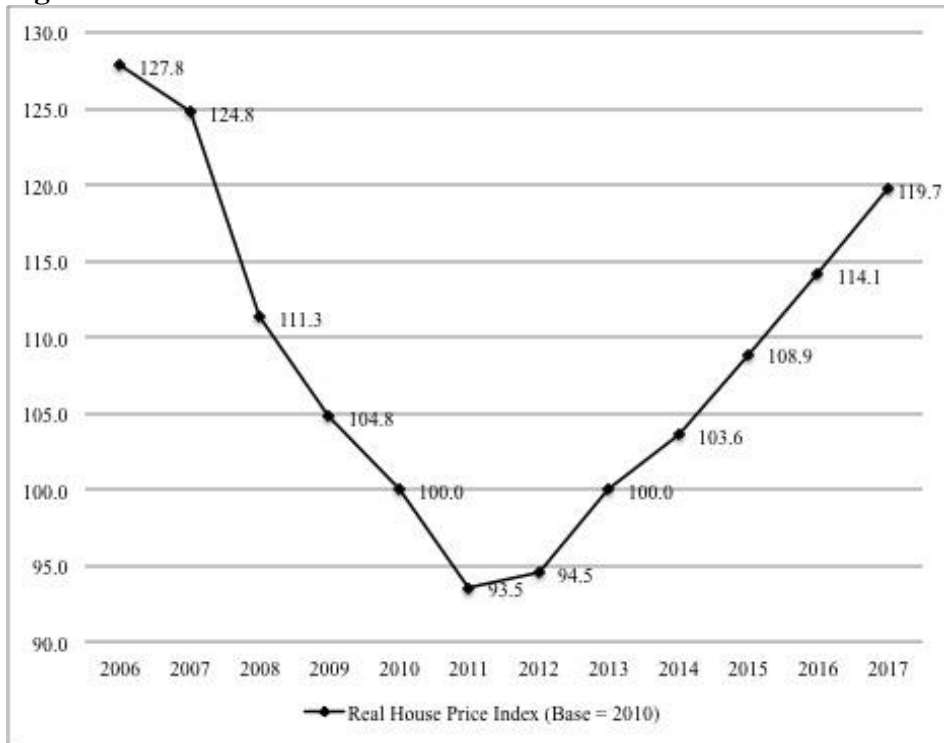


**Figure 1: Rent Price Index with Base Year 2010**



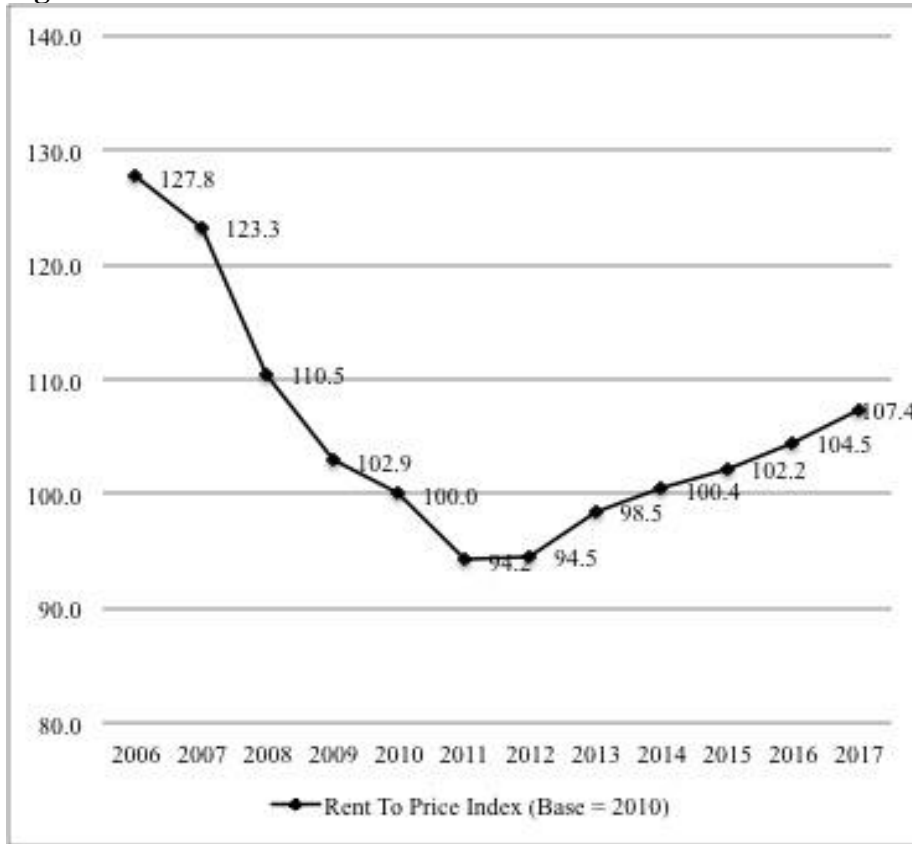
**Source:** OECD (2018), Housing (indicator). doi: 10.1787/63008438-en (Accessed on 20 February 2018)

**Figure 2: Real House Price Index with Base Year 2010**



**Source:** OECD (2018), Housing (indicator). doi: 10.1787/63008438-en (Accessed on 20 February 2018)

**Figure 3: Rent to Price Index with Base Year 2010**



**Source:** OECD (2018), Housing (indicator). doi: 10.1787/63008438-en (Accessed on 20 February 2018)

#### **IV. HOUSING SECTOR: THE DYNAMICS OF SUPPLY AND DEMAND**

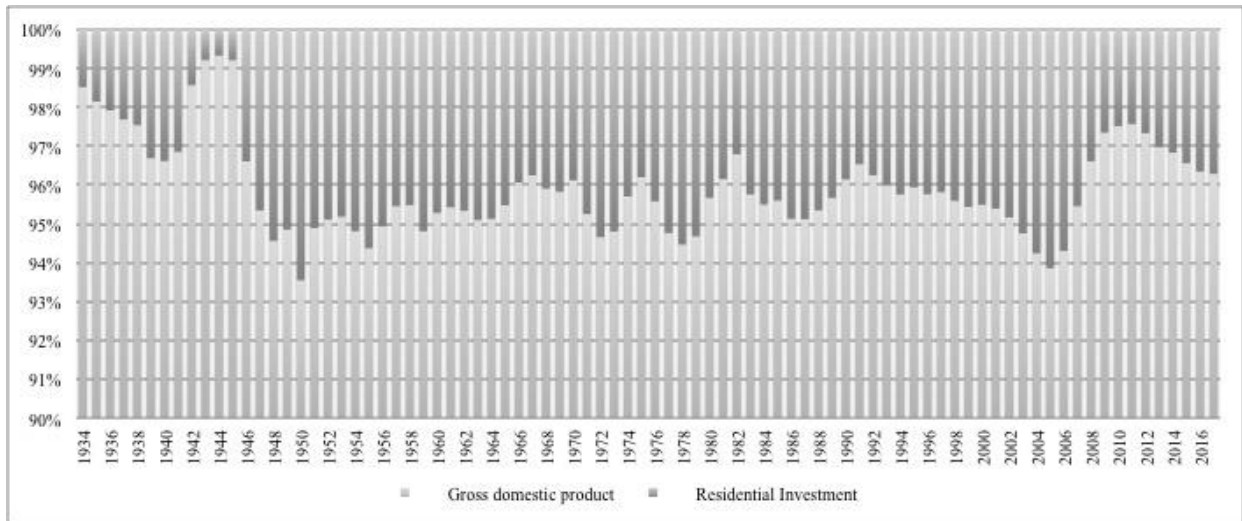
The basic policy tools employed by the federal government concerning housing aimed to increase the overall level of homeownership. Policies toward the latter part of the twentieth century were extended to promote residential construction and to increase homeownership amongst low- and moderate-income households. In line with housing policies first drafted in the 1930s, they focused on indirectly stimulating the demand and supply of housing in the economy, by promoting greater access to bank mortgage financing or providing tax credits to home owners and investors rather than directly intervening in the housing market to ensure that the ultimate goal of housing policy, as eloquently extolled by the Housing Act of 1949, that “every American deserves a decent home and a suitable living environment” is ultimately achieved (Lang and Sohmer 2000).

In spite of the focus of federal housing policy on homeownership and its importance on the dynamics of the macroeconomy, there is a dearth of academic literature associated with the macroeconomic view and impact of the housing sector on it. Leung's (2004) literature review on macroeconomics and housing highlights examples of this lack. He points out that publications such as the *Origins of Macroeconomics* by Robert Dimand, which cite the most important contributions to the field of macroeconomics from a wide range of economic scholars, only mentions Fisher's 1933 paper on debt deflation as having any links with the housing sector. Similarly in the *Landmark Papers in Economic Fluctuations, Economic Policy and Related Subjects* edited by Nobel Prize Laureate Lawrence Klein, lists only one paper out of a compilation of 40 selected papers, titled "The Relation of Home Investment to Unemployment" by R.F. Kahn, that relates directly to the housing sector.

On the other hand, the literature associating housing finance and the macroeconomy appears to be more exhaustive. Leung cites the example of the *Handbook of the Economics of Finance Vols. 1A-B*, edited by G. Constantinides, M. Harris and R. Stulz, which includes two macro-oriented papers that deal specifically with real-estate housing and the macroeconomy: "Consumption-based asset pricing" by John Campbell and the "Equity Premium in Retrospect" by Rajnish Mehra and Edward Prescott. The rest of the publication involves specific content that relates to the overlap between the financial sector and the macroeconomy. It is not a surprise that the overlap in academic research between finance and the macroeconomy is more prevalent than housing itself, considering that the main impact of fiscal policies concerning housing were primarily aimed at influencing the housing sector via the financial sector. The analysis of the effects of changes in the financial sector on the overall economy may therefore take precedence over the study of the impact of the housing sector on the economy.

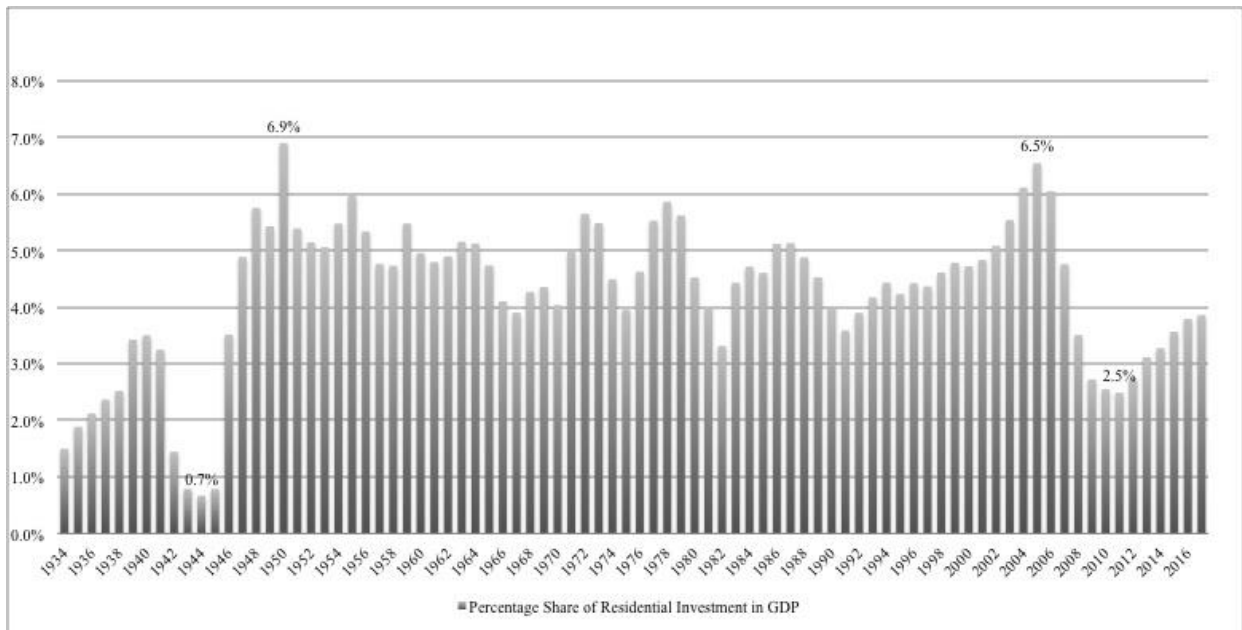
Even though mainstream economic theory may not have acknowledged the importance of the housing sector in the macroeconomy, its impact on major macro indicators cannot be ignored. This is simply because of the fact that the housing sector constitutes a significant portion of US GDP. The figure titled: "Residential Investment as a Share of GDP" below shows the trends of the share of residential fixed investment in GDP from 1934 to 2017, while the figure titled: "Percentage Share of Residential Investment in GDP" shows the percentage shares of the same.

**Figure 4: Residential Investment as a Share of GDP (1934-2017)**



**Source:** Bureau of Economic Analysis (Table 1.1.5. Gross Domestic Product)

**Figure 5: Percentage Share of Residential Investment in GDP**

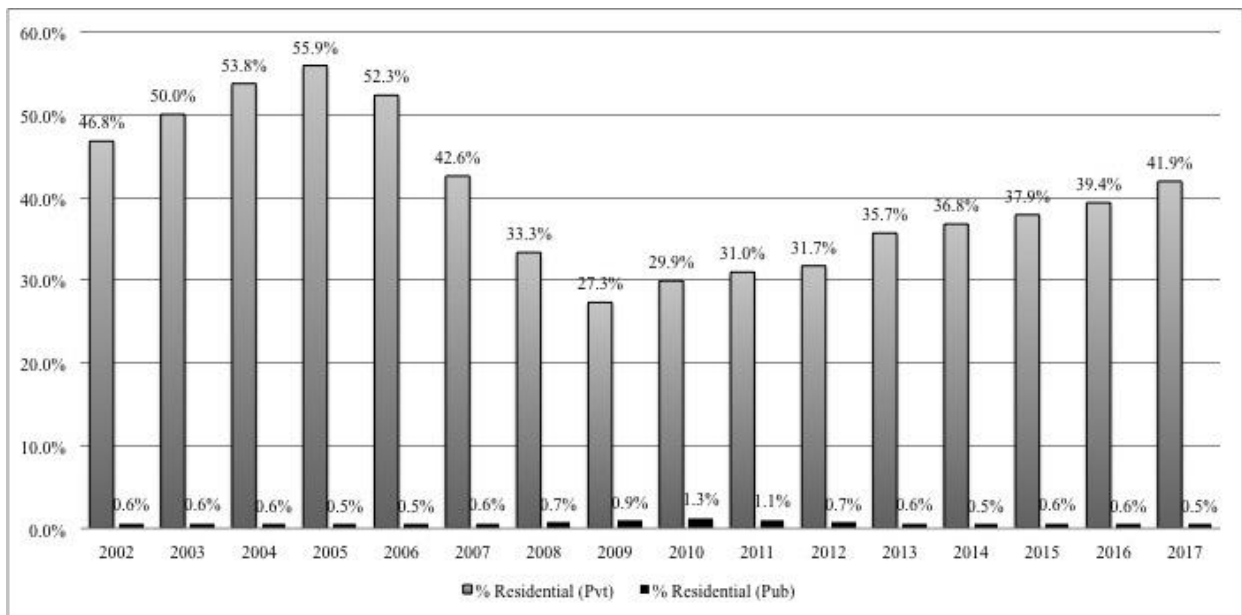


**Source:** Bureau of Economic Analysis (Table 1.1.5. Gross Domestic Product)

Since 1934, residential housing (excluding housing services) has constituted between 0.7 percent and 6.9 percent of GDP and on average 4.3 percent of GDP, declining to a 65-year low of 2.5 percent during the Great Recession. The stock of residential housing in the United States is composed of a) private sector owner-occupied and rental accommodation (single family and multifamily units) and b) publicly owned housing stock.

The most prominent source of housing at the national level originates in the private sector. This is evident from the trends in public and private expenditure on the construction of residential housing between 2002 and 2017 as shown in the figure below.

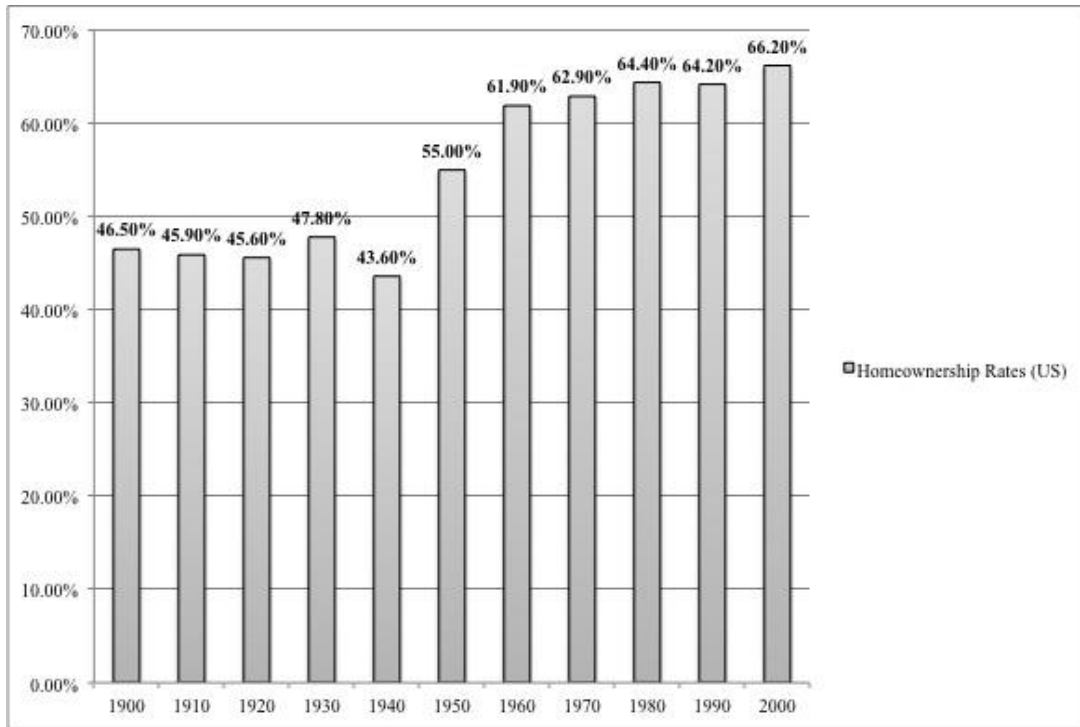
**Figure 6: Private Residential and Public Residential Construction as a Percentage of Total Construction (1993-2017)**



**Source:** Unites States Census Bureau (2018)

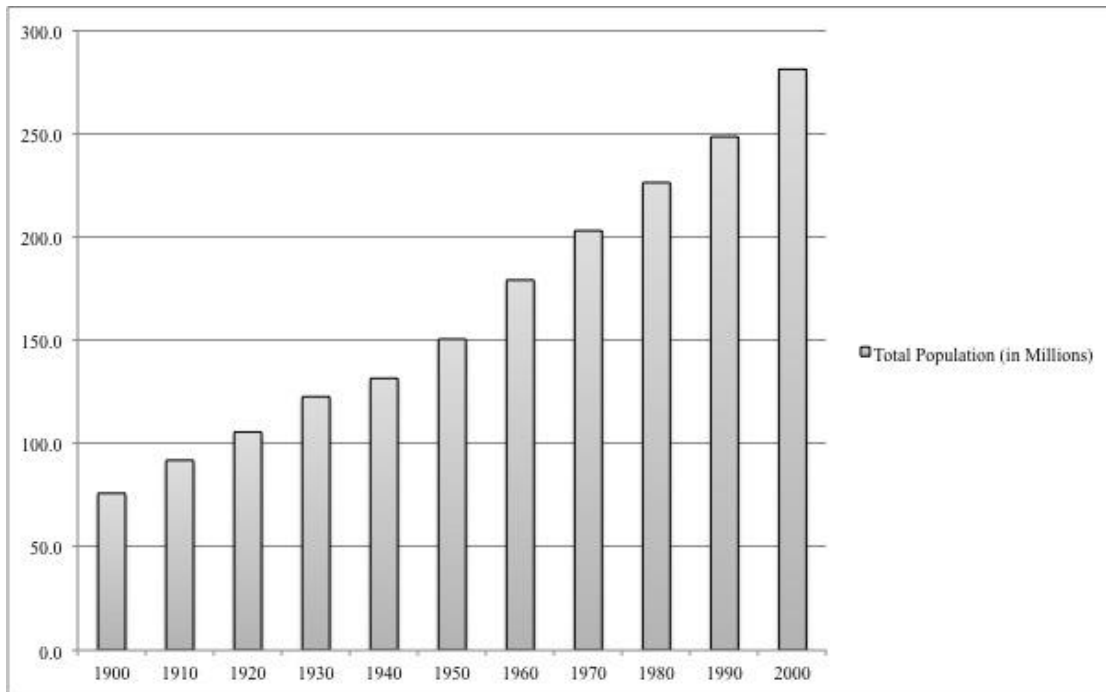
The figure above on private and public residential construction as a percentage of total construction shows that the proportion of public spending on residential construction out of total construction in the US economy is extremely low in comparison to that of private spending, indicating that the majority of housing demand clears through the private sector. The importance of the owner-occupied housing market in the overall housing sector can be understood by observing the trends in average homeownership rates of each decade between 1900 and 2000, in relation to the changes in national population growth over the same period, as represented in the figures below:

**Figure 7: Homeownership Rates in the United States (1900-2000)**



**Source:** United States Census Bureau, Housing and Household Economic Statistics Division (Last Revised: October 31, 2011)

**Figure 8: Total Population of the United States in millions (1900-2000)**



**Source:** United States Census Bureau, decennial census of population, 1900 to 2000.

From this data we get a sense of how homeownership has consistently been on the rise and in line with population growth over this time period. It can be surmised that for such an ideological perception of homeownership to not only sustain itself but to consistently gain traction over the years there must have been some form of reinforcing framework that carried it forward over the 20 century; especially during the post-WWII period and the time just prior to the Global Financial Crisis of 2007–09. This framework indeed presents itself in the form of the federal housing policy reforms that were enacted in response to the Great Depression in 1929, as seen above in chapter III.

### **The United States National Housing Sector: A Theoretical Overview of its Dynamics and Importance in the Macroeconomy**

As seen above, an often-cited point within the existing academic literature on housing is the lack of focus on its importance within the macroeconomy. Indeed it has only been in more recent years following the last housing-related economic crisis that more efforts have been undertaken to study the dynamics of the housing sector, in order to better understand the role of the varying endogenous and exogenous factors that determine how the aggregate housing market functions; some of the findings in this regard are reported in this chapter. As a first step however, it is necessary to highlight the importance of the housing sector in the macroeconomy, as a preface to the theoretical models that determine how the demand and supply of housing function.

The contribution of construction-related activity, especially residential construction, has a significant impact on the GDP of an economy via the output generated by construction-related jobs and the demand for construction-related capital (material and equipment) (Leamer 2007). The aggregate construction sector, inclusive of both residential and commercial construction, presents a unique characteristic; the sector follows a long wave cycle with an approximate duration of 15 to 25 years. Aggregate output growth tends to alternate between rapid and slow growth on a long wave cycle with intervals of 15–25 years. These long ‘swings’ in output tend to follow similar long interval swings that occurred at the same time in other sectors (Abramovitz 1964, 2). The volume of output generated through construction has followed cyclical patterns of roughly the same duration as the long swings in the rate of growth of aggregate output, especially in the sector of nonfarm residential building (Abramovitz 1964, 5). Abramovitz’s 1964 paper highlights that such observed long swings in output growth are the

result of swings in the rate of growth or resources and swings in the intensity with which these resources have been used, which in turn relate to effective demand in the economy.

Both of these factors have an important effect on capital formation, which influences the growth of production capacity as well as the growth of effective demand in the economy (Abramovitz 1964, 3-4). The capacity to produce is extended by gross capital formation through the introduction of substitutes for old technology; net increases of capital increase the productivity of labor. The growth of effective demand increases as the rate of change of gross capital formation increases either directly through an anticipated increase in gross investment expenditures or indirectly through the effect of any changes in investment expenditures on the growth of income and consumption. The construction sector possesses the unique capacity to influence capital formation in both of the ways described above: growth in the construction sector has a positive impact on both effective demand and the capacity to produce (i.e., the growth of resources) (Abramovitz 1964).

However in order for the residential construction sector to effectively serve this dual role of influencing capital formation, the housing market (i.e., the market in which the output generated by construction is bought and sold) should be based on a reasonably flexible price system to ensure that resources (labor and capital) are productively employed (Leamer 2007, 153). Unfortunately the prices of homes are rigid in a downward trending market. If effective demand in the market for homes (or even investments in residential property developments) dips, the adjustment in the market occurs at the volume level rather than the price level.

The inflexibility of prices is especially detrimental when the housing market is in decline, because the downward adjustment of volume in place of price, leads to a decline in sales and thus a decline in the jobs associated with construction, finance and real-estate brokerages (Leamer 2007, 177). If prices were less sticky the volume adjustment during a housing market decline that leads to less than full employment in residential construction and its affiliated sectors, could be avoided allowing the housing cycle to stabilize quickly back to normal sales volumes (Leamer 2007, 177).



This inflexibility in prices is seen both within the existing stock of housing as well as newly built homes. Current homeowners (sellers) are backward looking and being concerned with the price they have paid for their homes remain in a position of “loss aversion” (Leamer 2007, 177) by not risking the worth of what they have paid for their house in a weak market. At the same time prospective homeowners are forward looking in terms of the value appreciation that may occur in the real estate that they purchase. Thus in a rising market, sellers estimate that the value of their homes would be less than prospective buyers anticipate and decide to sell. On the contrary in a falling market sellers remember the price they originally paid to purchase the home while buyers anticipate ever declining prices as time progresses, leading to stagnation in both home sales and purchases (Leamer 2007, 177).

The weak price transmission mechanism in the residential housing market is counterintuitive to its role as a federal policy tool to establish stability within the economy. A macro stabilizer should ideally serve to regulate the trajectory of the economy in both explosive downturns as well as upswings, but as the case turns out, the residential housing market tends to serve this purpose only when the economy is in recession.

To see how this is let us consider first the dynamics of the owner-occupied housing sector in the specific scenario in which prices in the residential housing market are rising. The impact this will immediately have is to cause the economic prospects of investment in the supply of owner occupied housing to be increasingly positive as time goes by, prompting a rise in the rate of issuance of housing permits (starts), which in turn signals a rise in the potential number of new units that can be released for sale once the construction is complete at a later time period. This stimulates growth in the economic activity of owner occupied housing construction and its affiliated sectors, leading to higher employment and output generation within these sectors. Prices in the residential housing sector will continue to rise at a faster rate, evidenced by a consistent trend of higher than overall market rate of inflation during the upswing of the business cycle until it attenuates due an unsustainable level of inflation. But once prices in the residential housing sector (now comprising of both old stock whose prices have also appreciated in line with the current market price of new stock) have risen they tend to exhibit a rigidity toward decline, as would be seen in other sectors moving in line with the business cycle.

As explained above, this is mainly due to the fact that it is cheaper and faster for the supply of housing units to be controlled through the number of vacant units that are available for sale or rent; once the initial number of housing starts has spurred a boom in construction they will result in an increase in the number of vacant units that remain unsold or unrented rather than a physical decline in the total level of stock. Thus, when home prices were rising in the boom phase of the business cycle, the rise in demand for and sales of residential housing units would be absorbed by old units whose owners and prospective buyers agree on their backward and forward outlook on prices respectively, by old units that had previously remained unsold from previous boom phases in the housing cycle and by new units arising from the current boom in housing starts whose characteristics and prices matched the demand in the market for old units. The latter two groups of housing units comprise the set of vacant units that are available for sale and also apply in the context of rentals.

Thus it becomes clear that at the beginning of a boom in the housing cycle we may have a higher level of demand relative to the supply of physical housing units and as prices rise this stimulates construction to meet that demand, but towards the end of the cycle when the wave of construction of new units reaches completion and most of the old stock has been sold to meet rising demand that there would be a residual amount of new stock that contributes to vacancies in the next housing cycle.

On the other hand, when prices are declining, old stock remains intact (but unmaintained) while investment in the construction of new stock stimulated through new housing starts begins to dwindle to a level that existed before the boom or perhaps even lower based on what the expectations of house prices will be, meaning that supply remains relatively inelastic in the face of changing prices, leading to a loss of jobs and contraction of the residential construction sector. The demand for owner-occupied housing (across both old and new units) by buyers remains high in a declining market but if suppliers (owners) of owner-occupied housing are unwilling to sell at prices that are not sufficiently above their actual purchase price they will hold on to their homes and not sell.

This simply means two things: that there is no new stock being invested in to meet the relatively high demand for owner-occupied housing in a declining market, and that potentially, owners of old units do not release their units into the available supply; leaving a gap in the effective demand for owner-occupied housing (a sort of latent level of effective demand that serves as the substrate for the next housing cycle stimulated by demand –led policies).

In order to have a full understanding of the dynamics of the housing sector we must also address the rental sector and not just the owner-occupied sector in isolation, because rented units serve as the direct substitute to owner-occupied housing (Riddel 2004, 124) for a vast majority of those who demand owner-occupied housing when they can afford it. The stock of new rental housing in any time period is supplied by those who chose to invest in the construction of multifamily units or single-family units specifically for the purpose of renting in a prior period, while the existing stock of rental housing serves to meet the demand for rental housing in the short run. The changes in the demand for rental housing may in part be viewed as a residual of the demand for owner occupied housing; income shocks or a sudden spike in user cost or the cost of maintaining an owner-occupied home may result in home-owners trading down or losing ownership of their homes through default on their mortgages, resulting in a sudden spike in the demand for rentals in the short run. The latter however is representative of a subset of the demand for rental units that overlaps with the demand for owner-occupied housing where the preference remains for owner-occupied housing provided household budget constraints are less restrictive.

Another and perhaps more substantial subset of the rental demand is represented by households who are in the middle income bracket of the population, whose demand for rental units between geographical areas (where the cost of moving between these areas is negligible) tends to be either more price elastic or income elastic in the short run. In other words, for example, a small increase in the rents in area A because of gentrification will lead to a large increase in the demand for rental units in area B where the rents have not been impacted by gentrification. The remainder of the demand for rental units comprises those who are in the low-income category of households, especially those who require the use of welfare assistance (such as housing vouchers) to afford to rent their homes. Interestingly, a paper by Malpezzi and Vandell (2002) on whether or not the low income Housing Tax Credit (LIHTC) program led to an increase in

the supply of housing, indicated that the income elasticity of demand for housing, which by assumption should be rental housing for low-income households, tends to be relatively low; in other words the relatively sizeable increases in purchasing power from such allowances results only in minor increases in spending on housing.

As in the previous example, consider a scenario where the prices of owner occupied housing are rising, how would this impact the demand and supply for rental homes in the long run? Gallin (2004) shows through the use of a long-horizon regression approach to a standard error correction model that in a scenario where housing prices are rising (i.e., that they are high relative to rents and the rent to price ratio is low) changes in real rents (price deflated nominal rents) tend to be larger than usual and changes in real prices tend to be smaller than usual. Gallin's premise is that there should not be a significant difference between the appreciation in housing prices and rents, given that both depend primarily on the user cost (which in itself is a function of the marginal tax rate and interest rate). But his findings indicate that between 1994 and 2004 (just before the great financial crisis) nominal house prices increased by 70 percent but the indexes for tenants and owner's imputed (equivalent) rent in CPI shows that it had increased by less than half as much, which is counter-intuitive since imputed rents are considered a fundamental determinant of housing value, so prices and rents should be more or less in line with each other. His other findings include the fact that periods in which house prices are high relative to rents appear to be followed by periods in which the real rent growth is faster than usual and real house-price growth is slower than usual and that the response of prices dominated that of rents.

It is interesting to note that these findings were based on data from the period just prior to the Global Financial Crisis; a time when the mortgage lending market was beginning to change its approach towards moderate and low-income households and when both the Clinton and Bush administrations enacted policies that expanded the base of low-income homeowners, resulting in a supernormal rate of increase in housing prices just prior to the great recession. The model would however have accurately predicted the period of faster real rent growth following the crisis given that the large number of foreclosures on low-income owner-occupied homes would have resulted in a spike in the demand for rental housing, with the simultaneous slowing down of real house price growth without the dominating effect of price on rent in this special instance.

Unfortunately the model makes no specific mention of the distribution of income between households that rent and households that own homes. This is an important distinction, discussed further below, given that the impacts, and the subsequent outcomes, on the demand for rental units and the demand for owner-occupied housing under conditions of inelastic short-run supply tends to vary across the income distribution of households, especially in the wake of a demand-led policy approach used to stimulate the macroeconomy.

### **External Factors That Impact Short-Run Demand and Supply Other Than Prices**

The general discussion of the dynamics in the housing sector typically begins at the point where housing prices are already either rising or falling. As we have seen so far, the downward rigidity in the price mechanism results in volume adjustments to arrive at a new equilibrium. Thus while price disturbances are relatively slow to catch on in the short term how then is the housing sector stimulated to move up without the aid of price signals? This is the question we addressed in this section.

Refer to the previous example in which housing prices are rising. This is an indicator of stable macroeconomic growth and also therefore of rising inflation (including a much more rapid increase in inflation in home prices). However the rise in overall inflation (which is strongly influenced by inflation in the housing sector) is a phenomenon that needs to be controlled in the short-term; in other words over a time horizon that is more restricted than the natural rise and fall in volume adjustments in the supply of housing. To curb the rise in inflation during a business cycle and housing market upswing, monetary policy raises short-term interest rates, increasing the borrowing costs to both suppliers of new housing units (affecting expectations of housing supply) as well as the user costs to buyers of both existing and new owner-occupied units. These effects in turn impact the expected returns on investment in owner-occupied housing (both from the suppliers' in the immediate future and buyers' perspectives further into the future) as changing interest rates begin to alter expectations of future house-price movements (Mishkin 2008). Thus the transmission mechanism of monetary policy takes place through the housing market.

There are two other factors that are not related to the cost of construction that impact the supply of housing: the mismatch between the availability of land and areas where individuals have a higher than normal preference to reside (usually areas that are highly developed metropolitan areas) and land use restrictions (Mishkin 2008). In the case of the former, unoccupied land that is easily and readily available for development may not be desirable whereas the converse is true in more highly desirable urban areas where employment opportunities and amenities are relatively more abundant. The general long-run equilibrium model of the housing sector assumes that an increase in prices will lead to an overall increase in investment in residential construction (*ceteris paribus*), with such a model implying that high price levels imply high levels of investment in construction. However in reality the existence of restrictive land-use regulation can in fact slow the growth in housing stock. Land-use restrictions therefore limit the number and size of residential structures that are permitted within any given lot. This implies that the elasticities of supply through vacancy adjustments vary between areas as a result of these two key factors (Mishkin 2008; Riddel 2004; Green Malpezzi and Mayo 2005 and Malpezzi and Vandell 2002).

Other sources of demand disturbances that act in the short run according to Riddel (2004), are changes in marginal tax rates, changes in household consumption behavior, tastes and preferences for home size and location or other amenities, stock market volatility and the preferred composition of household financial portfolios for long-term versus short-term investments. Supply disturbances would be, supply-side shocks rapid changes in building material costs / changes in international trading agreements, changes in construction employment, wages through labor mobility, change in lending rates for construction and development loans.

Given this general presentation of the operation of the housing sector operates over the long cycle and the observed factors that influence the demand and supply in the short run when the price mechanism is relatively unresponsive, the next step is to understand the framework that condenses these points into a long-run equilibrium model and how such a model explains the asymmetry between demand and supply in the housing sector.

### **Long-Run Equilibrium Demand for Housing**

According to existing housing demand theory, long-run equilibrium demand for current housing, is a function of price and a set of demand variables such as income and long-term interest rates. Riddel (2004) uses this as a basis to develop a model for the disequilibrium of the housing market (and uses data on single-family units between 1967 and 1998 to test the model). The model sets prices, housing stocks, residential rents (including imputed rents), construction costs and vacancy rates as nonstationary endogenous variables while the economic growth rate, interest rates, income and the stock of multifamily units are exogenous variables. Application of the model on the chosen set of data found that the income elasticity of demand for single-family units is approximately 2.7 and that the long-run elasticity of demand is approximately 2.8. Surprisingly, Riddel's results show that user cost is not a significant determinant of long-run housing demand, but, as seen earlier, is more effective in influencing demand decisions in the short run. The mean rental elasticity is 0.27, meaning that 1 percent drop in rents leads to a 0.27 percent increase in the demand for owner-occupied housing. Rental elasticities tend to be higher for those households that face stricter borrowing terms than those that do not and in general tend to also be lower than the price elasticity of demand. In the case of the latter, we can assume that it may be easier to trade up/trade down between owner-occupied homes than it is to move between rental agreements due to penalties on breach of rental agreements and to moving costs that add up to a higher proportion of income for renters than the average homeowner. In the long run therefore, the strongest determinants of housing demand overall are income and price and to a lesser extent rents, and the eventual price appreciation and changes in interest rates affect the flow of new investment in housing demanded rather than the stock. A highly relevant finding that Riddel emphasizes is that interest rate changes do not have a significant impact on the demand for housing of existing homeowners but it did have a significant impact on those entering or leaving the market and those who were entering the market as first-time homeowners – thus they have a stronger impact on new investment flows rather than on existing stocks.

### **Long-Run Equilibrium Supply for Housing**

The basis for the supply theory of housing as outlined by Riddel (2004) is that housing which is a durable good constitutes a market that has both a flow dimension and a stock dimension. Increases in the new investment of housing stock contribute to the flow of housing stock in any

time period, and therefore net investment, which is the difference between the sum of new residential construction and the depreciation of existing units, becomes the primary focus when attempting to stimulate growth in the housing sector. According to Di Pasquale and Wheaton (1994), the supply theory of housing assumes that the long-run equilibrium in the supply of housing stock is dependent on price and a vector of other cost-shifting variables, already encountered above. Thus, housing investment or new construction is directly related to the price level and an overall increase in the price level leads to permanent increases in new construction. Riddel's model found that the long run price elasticity of supply was between 0.025 and 0.49, in line with other similar studies conducted. However Goodman (2005) shows that supply elasticities in central city areas (where land use restrictions are stronger) vary significantly based on whether the flow of housing units (new units) are either increasing or decreasing. Goodman finds that supply elasticities of the flow of housing in declining cities were between +0.03 and +0.13 (relatively inelastic) but that for expanding cities the elasticities of supply of the flow of housing were between +1.05 and +1.08 (relatively elastic), indicating an asymmetric or "kinked" supply response in the new investment in housing stock depending on whether the rate of new investment is either increasing or decreasing (Goodman 2005, 332).

### **The Dynamics of the Aggregate Housing Market: a Summary**

Thus, over the long cycle of the housing sector, demand for housing is most responsive to interest-rate changes and price changes but in the short run, once prices have increased during a housing sector upswing, they remain rigid in the downward direction, with volume adjustments in new investment and a slowing down of the sale of existing stock taking place to enable the market to reach a temporary equilibrium that becomes disrupted by another supply or demand side factor. Thus price adjustments in line with demand or supply occur over a longer period more coherent with the long wave of the housing cycle and so price appreciation and changes in interest rates tend to impact the flow rather than the stock demand of housing. Rents have a lower impact on the decision to invest in owner-occupied housing. Thus, because of the continuous disruption that exists in the short run, there is an inadequate level of adjustment in prices and the housing market supply and demand remain in disequilibrium, with extended periods of either excess supply or demand. Supply in the short run, however, is even more inelastic than demand because of limitations on land-use rights and differences in preferences of where households choose to live in relation to the availability of land that can be developed, and



so also contributes to the lack of responsiveness of supply to changes in price in the short run. In the long run there is also asymmetry within the supply of new investment in housing (based on whether new investment is occurring at an increasing or decreasing rate) that renders the supply of new housing asymmetric, making long-run equilibrium between demand and supply even more difficult to achieve in areas that are in decline, where new investment is less likely to occur but demand may still be fairly high in comparison to the available stock.

### **The Impact of Demand-led Federal Policy on the Dynamics of an Asymmetric Housing Market**

Having understood the dynamics of the housing sector in terms of how demand and supply are modeled and what factors impact them over the long swing housing sector cycle, it is clear that the asymmetry that exists is based on factors that impact prices disproportionately between supply and demand; prices are more responsive to demand-side shocks than supply-side shocks, whereas the adjustment of the volume of housing stock is solely responsive toward supply side shocks (Riddel 2004). This may be why the analysis of the impacts of such shocks is studied in isolation from each other.

However, apart from the existence of this asymmetry, a downward trend in the housing sector first generates adjustments in the employment of resources such as labor and capital to reduce the rate of growth in the volume of stock (because existing stock cannot be diminished and projects tend not to remain incomplete but spread over a longer horizon). Similarly, to stimulate growth in the employment of capital and labor associated with the construction sector that would follow a long swing cycle, the growth in volume of new stock needs to be stimulated, given the varying restrictions associated with land use and other non-price related factors that introduce rigidities and inefficiencies in the market in the short term. The latter explains the main goal that federal housing sector policy initiatives have focused on achieving, and the simplest way to achieve this is by reducing the budget constraints of investors and the end consumers of residential housing, through changes in marginal tax and interest rates.

Of course investment decisions (to enter into construction of both owner occupied or rental units) are dependent on the level aggregate demand there is in the housing economy, but this is now highly dependent on the level of user cost associated with homeownership as well as the

expectation of positive wealth effects in the future for potential homeowners. However, wealth effects cannot be impacted positively without a more flexible price mechanism in combination with lower user costs, and since the prices respond primarily to demand-side disturbances, the simplest policy tool that the federal government can employ would indeed focus on demand-side measures that are tied to the reduction of household budget constraints and constraints on housing investment (expansion of household income through wider access to expanded mortgage credit and reductions in marginal tax rates or interest rates). However this bias towards demand-led growth-promoting strategies without the aid of countercyclical policies to support the housing sector in times of a down-side have negative impacts that affect households at different levels along the overall distribution of income differently, which will be elaborated upon in the next section. Thus demand-led housing policy based on Keynesian pump-priming principles makes the housing sector as it exists and is governed today, more of a macro-economic stimulant than the macro-economic stabilizer that it ought to be.

### **What is Missing From These Models/Analysis of the Housing Sector?**

Most studies undertaken to explain the dynamics of the housing sector tend to focus on only specific parts of the sector, such as owner-occupied housing or rental housing independently, or to focus their analysis on the specific impact of a piece of housing-related legislature on either owner-occupied housing or rental housing. Even formulating a coherent model of the housing sector that encompasses all the constituent elements of housing demand and supply is difficult, simply given the nature of the good itself— a long-lived, durable good whose purchase in the modern-day housing market is largely not possible without mortgage debt and whose supply is restricted by non price related variables such as land use restrictions.

However an important aspect of modeling the housing sector that is not particularly covered in analysis is the dual role that housing plays as a capital (investment) good and as a necessity good. While the purchase value of owner-occupied housing is accounted for in GDP as a capital investment, any imputed rents from the house are now accounted for as a consumption component. However this dual role that owner-occupied housing plays has more far-reaching effects in the economy. An owner occupied unit serves not only as an investment in the form of a long-lived asset that helps to generate wealth effects in a rising housing market, it is also the owner's primary source of shelter and stability— a place to raise a family, a primary necessity to

safeguard other assets, and forms a basis for further consumption in the form of goods and services that add to a basic standard of living. The effects on the demand and supply of owner-occupied housing have an impact on rental housing which becomes its direct substitute when the housing market is in decline. The consumer of rental housing, which is entirely a normal good and does not possess the characteristics of an investment good like owner-occupied housing, is more likely to be on the lower end of the income distribution and thus more susceptible to effects of demand-shocks introduced by demand-led policies in a capital constrained housing market in the short run.

## **Conclusion**

From the above, we can infer that it appears easier and more fruitful in terms of overall growth to jump-start the economy at large by leveraging the growth in the residential construction sector, irrespective of where the demand for owner-occupied housing lies. Fiscal policies that impact user cost, the main decision factor in homeownership and monetary policies targeting the expectations in housing prices prove effective in achieving this jump-start where actual long-wave price fluctuations that follow the housing cycle appear sticky over the short-run timelines that these policies tend to follow. So when the economy is in need of a short-term burst of significant growth a pump-priming strategy to get residential construction going is the simple, most balanced budget-friendly and liberal mechanism that can be adopted. The New Dealers definitely seemed to think so and drew up housing policy that promoted home-ownership as the fundamental utility maximization objective of every contributing economic agent at the time (simply by reducing their budget constraints through credit creation and a higher level of accessibility to mortgage financing). But what served as a fundamental objective at that point in time is not one that should continue to do so in an economic environment and time when the dynamics of home ownership are rapidly changing. The reasons for this will be discussed in the next section.

## **V. FEDERAL POLICIES IN AN INEFFICIENT HOUSING MARKET AND ITS IMPLICATIONS**

The examination of the origins of federal housing policy in the United States in Chapter III has demonstrated a bias towards homeownership, as well as a bias towards the use of the housing sector as a basis for countercyclical macro policy. The last chapter demonstrated how the housing market is subject to inefficiencies caused by the asymmetry in housing supply as well as the short-run disequilibrium between housing supply and demand. The biased use of demand-side macro policies in an inefficient market tends to worsen the disequilibrium between demand and supply that in turn tends to negatively affect households on the lower end of the income distribution than those on the higher end. In the long run this could predispose a number of such households to the threat of homelessness unless measures are taken to plug the short-term gap in supply that is generated by the market disequilibrium.

Federal policies that promote homeownership would be beneficial to those households that can afford to trade up from renting to ownership, or from owning smaller owner-occupied units to larger or more units. Such households tend to exist within the upper end of the income distribution and are less likely to be negatively influenced by fluctuations in the factors that adversely affect affordability of housing. On the other hand, as we shall see below, households at the lower end of the income distribution tend to be more likely to be impacted in the short run by affordability problems, but that the mitigation of these problems through the current set of federal housing assistance programs designed for low-income households is relatively ineffective in an economy where there is a widening gap in low-income housing supply. The rest of this chapter clearly investigates how the focus of government policy in mitigating distributional problems associated with affordability of housing for low-income households and how such an approach needs to be extended to accommodate more supply-side measures.

In the decades following the New Deal era when the first major housing policy reforms were enacted by the Federal government, a variety of policies and programs aimed at improving the overall distribution of housing across all income groups were introduced. However the dominant approach of most federal programs has shifted from the direct provision of affordable housing to the enhancement of affordability of housing through rental assistance and subsidy programs,

which are more prevalent today than programs associated with provision of public housing. This shift in approach has resulted in a decline in the overall supply of housing and in turn has rendered the programs designed to improve affordability of housing less effective; without a sufficient number of units to absorb spikes in effective demand (when the economy is improving) changes in affordability would not have as much of a positive effect as when there is enough supply to clear the market. Without adequate direct government intervention that supports the provision of a higher number of affordable public housing units to fill the gaps in an already inefficient private housing market, the supply needs of housing for shelter will not be met for a set of households who may not be able to benefit from affordability programs quick enough to prevent them from becoming homeless; it is these households who are more in need of housing as a primary source of shelter and most susceptible to losing access to it when the housing market fluctuates as a function of demand-led fiscal measures.

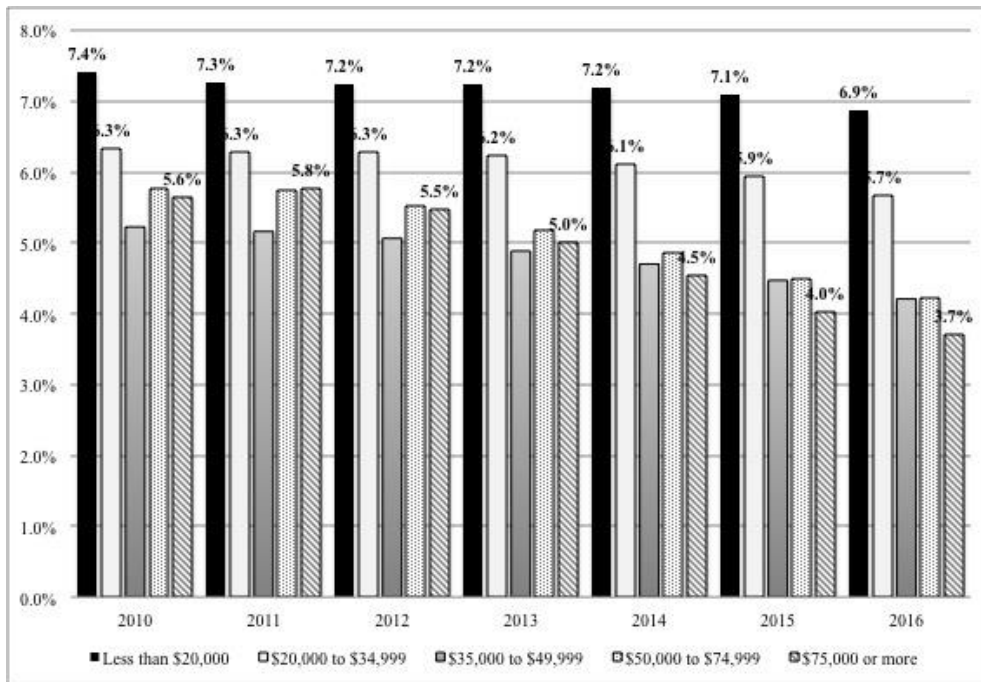
### **The Affordability Gap**

The current government policy to reduce inefficiencies in the distribution of housing among low-income households is to shrink the affordability gap. To understand this policy approach, it is necessary to define the affordability gap and how it is determined. Affordable housing may be defined as expenditure of not more than 30 percent of a household's income on housing costs ([ICPH] 2015, 103). Factors that impact affordability are quite disparate and make it difficult to generate a unified model of housing affordability; the distribution of housing prices and quality, distribution of income, the conditions affecting the supply of new and the refurbishment of old housing, consumer choices, the ability of households to borrow, and public policies affecting the housing market all play an important role in determining the affordability of housing for any household (Quigley and Raphael 1994).

Affordability also varies according to whether a household owns their home or rents. For homeowners the concept of affordability is based on the contractual terms of purchase of the unit and on how the loans used to purchase them are amortized. For renters on the other hand affordability refers to the terms of their rental agreements and the ways in which rent relates to income (Quigley and Raphael 1994). Figures 9 and 10 below indicate how households that rent face a higher burden in terms of the proportion of income spent on housing costs than households that live in owner-occupied units. On average between 2010 and 2016 only 7.2

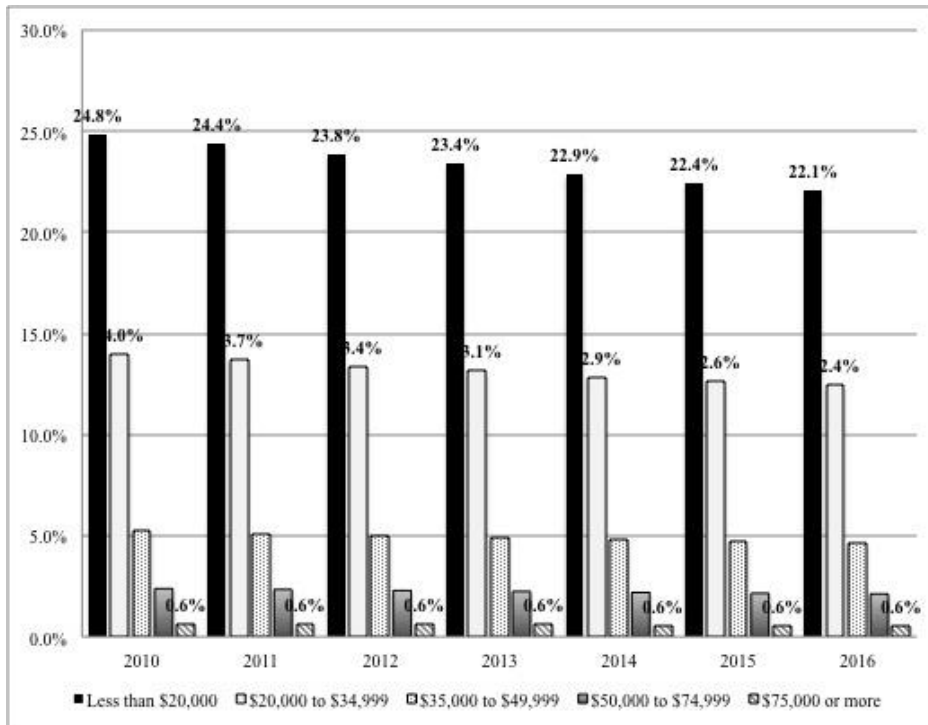
percent of homeowners in the lowest income bracket faced housing costs above 30 percent of their income. This figure is even lower for households in higher income brackets. However, on average 23.4 percent of renter households in the lowest income bracket faced housing costs above 30 percent of their income, indicating that affordability problems are more likely to be prevalent amongst low-income renter households.

**Figure 9: The Percentage of Owner Occupied Units above Affordable Housing Threshold by Household Income**



**Source:** U.S. Census Bureau: 2012-2016 American Community Survey 5-Year Estimates, 2011-2015 American Community Survey 5-Year Estimates, 2010-2014 American Community Survey 5-Year Estimates, 2009-2013 5-Year American Community Survey, 2008-2012 American Community Survey, 2007-2011 American Community Survey and 2006-2010 American Community Survey

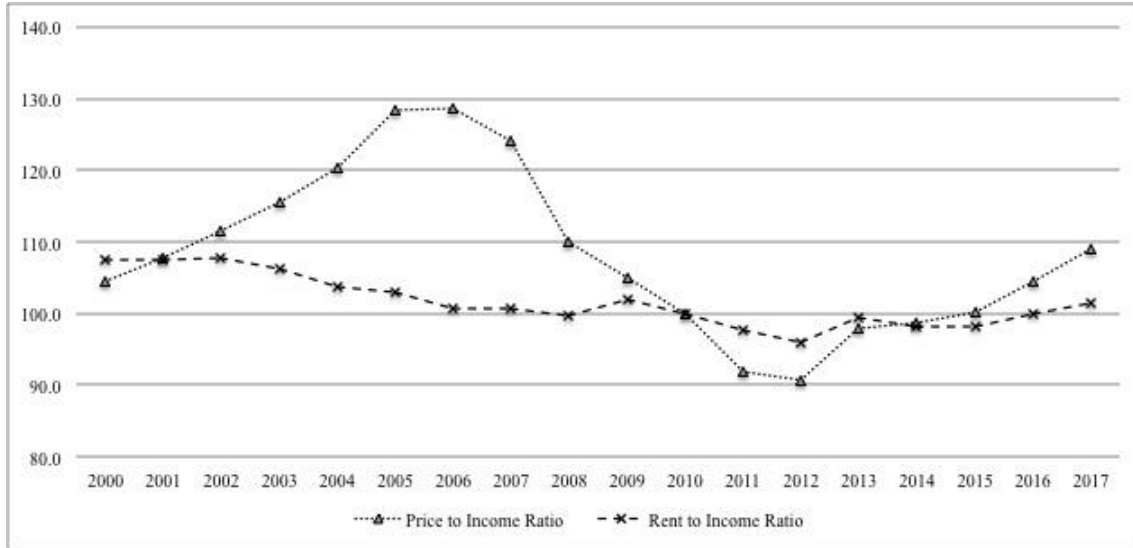
**Figure 10: The Percentage of Rental Units above Affordable Housing Threshold by Household Income**



**Source:** U.S. Census Bureau: 2012-2016 American Community Survey 5-Year Estimates, 2011-2015 American Community Survey 5-Year Estimates, 2010-2014 American Community Survey 5-Year Estimates, 2009-2013 5-Year American Community Survey, 2008-2012 American Community Survey, 2007-2011 American Community Survey and 2006-2010 American Community Survey

Additionally Figure 11 below indicates the ratios of price to income and rent to income between 2000 and 2016. We can see that just prior to the sub-prime mortgage crisis in 2005–2006 the price to income ratio is at its highest, while rent to income is comparatively very low. This indicates that the housing boom, supported by increased lending to lower income households contributed to a dramatic rise in the price to income, while low rents kept the rent to income ratio low during this period. In the postrecession years from 2014 onwards we are now seeing both the price to income and rent to income rates rising, although the former appears to be happening faster than the latter.

**Figure 11: Price-Income Ratio versus Rent- Income Ratio (2000-2017)**



**Source:** OECD (2018), Housing (indicator). doi: 10.1787/63008438-en (Accessed on 20 February 2018)

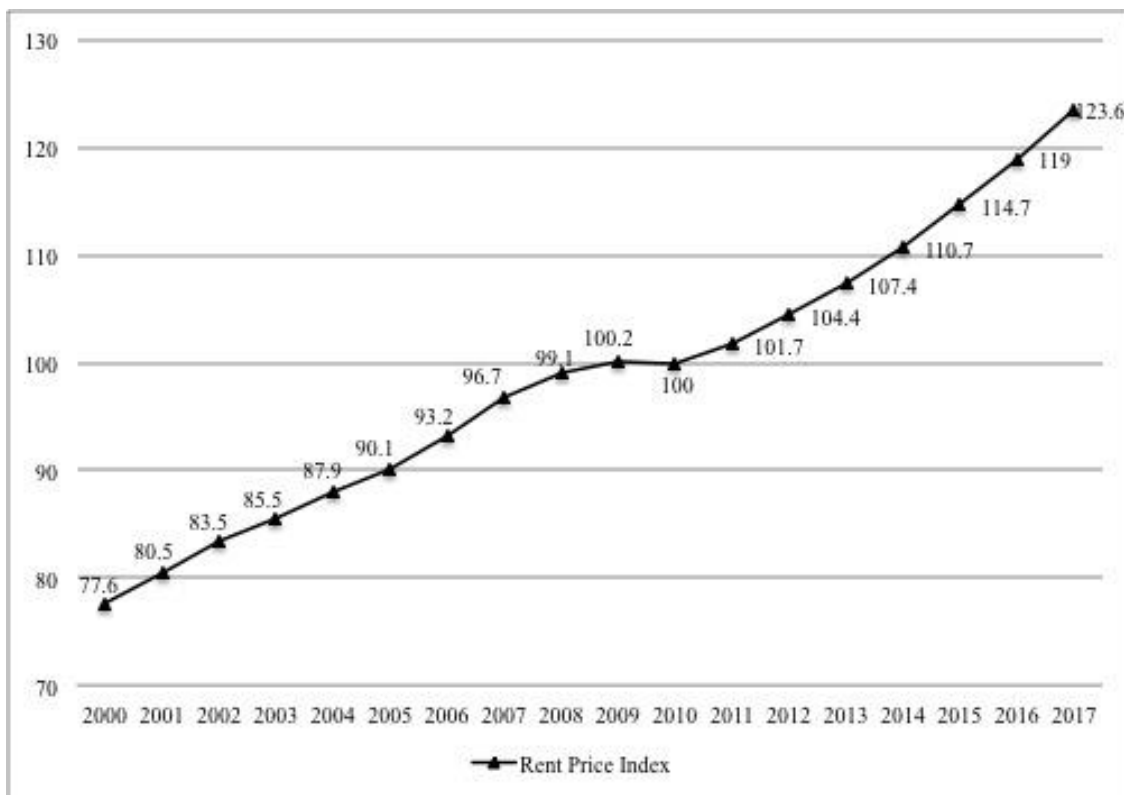
Quigley and Raphael also state that based on their findings in their 2004 paper that the affordability by homeowners, who in the United States are the majority among households, has not declined since the 1970s but that for the remaining set of housing consumers, who are renters, even though the share of expenditure on rent for the median renter had only increased marginally, the rent burden for poor and near poor households had increased dramatically over the same time period. From 1960 to 2000 the rent to income ratio for the median renter in the bottom income quintile increased from 0.47 to 0.55 and the proportion of households spending more than 30 percent of their income on rent increased from 0.62 to 0.79. At the same time increases for households in the middle quintile were negligible and for those in the top quintile were more moderate (Quigley and Raphael 2004).

One explanation for this may be, as seen earlier, that federal policies adopted under the Clinton and Bush administrations in the 1990s and early 2000s helped increase affordability of homeownership for low-income households through favorable tax reforms, lower lending restrictions, and community reinvestment initiatives in the period just prior to the Global Financial Crisis. When the crisis ensued in mid-2009 it led to a mass wave of foreclosures on the majority of newly generated low-income home mortgages and a correction in terms of the ‘heightened’ level of affordability of homeownership.



With these foreclosures came an increase in the demand for rental units as homeowners who had lost their primary source of shelter now needed to shift to the rental sector to find housing. The shift in rents that had occurred during the pre-recessionary housing boom continued to increase following the crisis as demand for rental units increased and a shift in investment patterns moved new residential construction towards building to rent rather than for sale. Below is a figure of the OECD's "Rent Price" Index data from 2000 to 2017, with base year set at 2010. The index shows that rents have increased by at least 24 percent between 2010 and 2017.

**Figure 12: Rent Price Index (2000-17)**



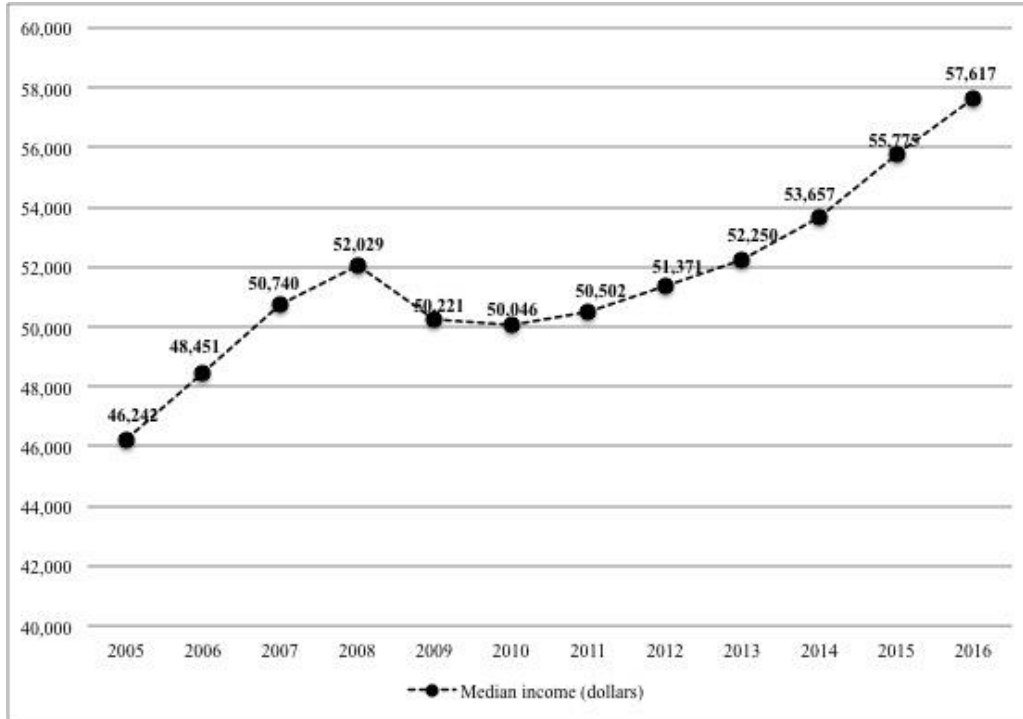
**Source:** OECD (2018), Housing (indicator) (doi: 10.1787/63008438-en (Accessed on 24 April 2018)

However there has not been adequate expansion in the necessary rental assistance programs, to improve housing affordability for low-income households, leading to states having to finance the shortfall through other means ([ICPH] 2015, 103).

The trends in median household income between 2005 and 2016, as seen in figure 13 below, indicate that income has been rising very slowly in the years following the recession; from 2005 to the start of the recession in 2008 the median income grew approximately at an average annual

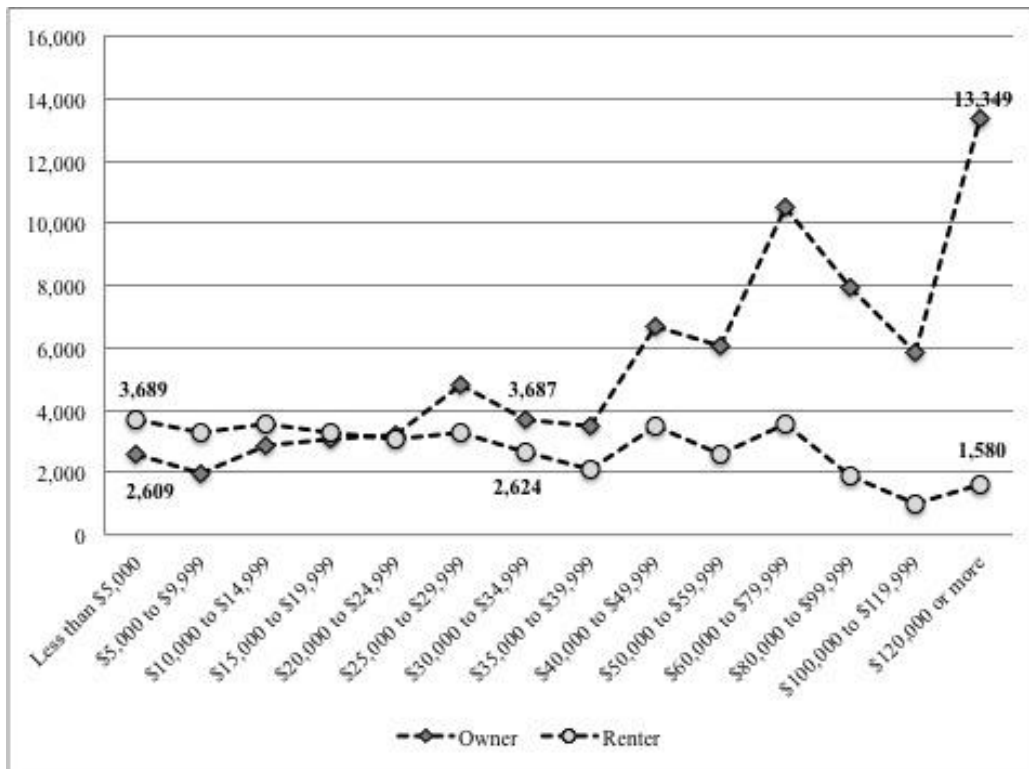
rate of 4.2 percent, whereas between 2010 and 2016 this dropped to 2.5 percent. In a post-recessionary environment where incomes are not rising as quickly as housing rents, the affordability gap for low-income households – including those availing of rental assistance is increasing. Figures 14, 15 and 16 below indicate on average the number of owner-occupied and renter-occupied units in each income bracket for the years 2011, 2013 and 2015. The data indicates how the number of owner-occupied units compared to rented units is decreasing over this time period. In 2011 households were more likely to purchase a home rather than rent if they had an annual income above \$25,000. In 2013 the gap between renters and owners remains fairly small for households with an annual income of \$25,000 to \$40,000 before starting to increase more significantly and in 2015 the renter to owner gap reduces even further for households with annual incomes between \$25,000 and \$40,000. This decline in the number of households with relatively lower annual incomes, purchasing homes could be the result of changes in demographic tastes (e.g., among Millennials) or it could be the result of high owner-occupied unit prices relative to income. Given the fact that bank financing of mortgages has become more restrictive and that incomes are not growing as fast as they did prior to the recession, this shift may be an indicator of a lower level of affordability of homeownership during this period, rather than changing preferences. While it has been shown that factors impacting affordability are different for homeowners and renters, the fact that more lower-income households are opting to rent will eventually lead to rents growing at a faster rate than incomes or rental assistance and this will eventually lead to affordability issues for renters, unless they can easily shift to being homeowners again.

**Figure 13: Median Income (2005 –16)**



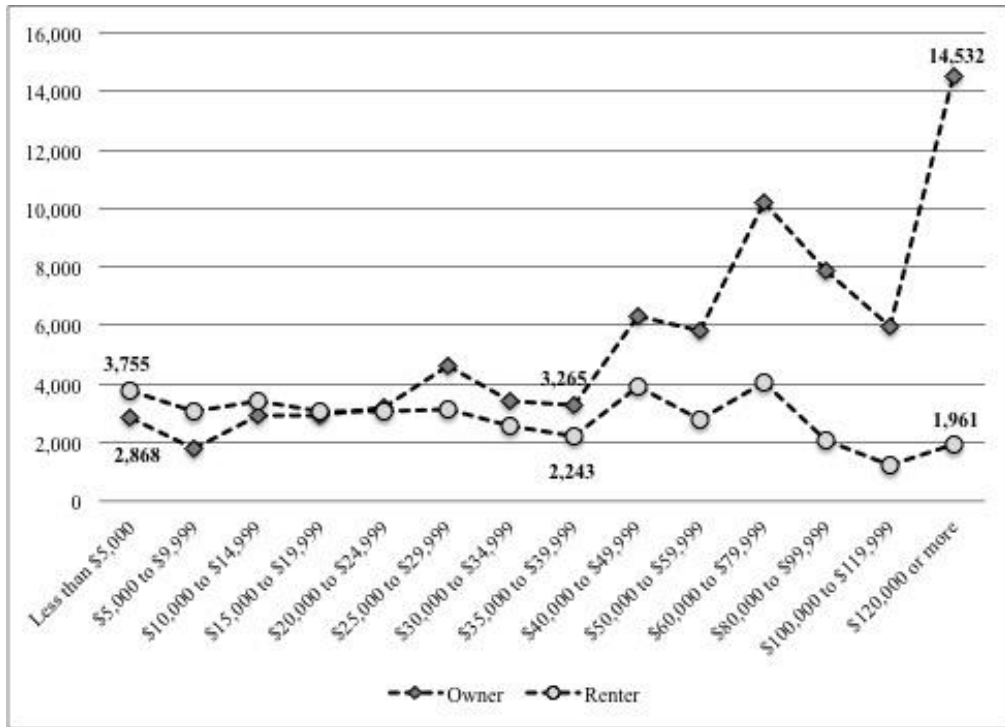
**Source:** U.S. Census Bureau: 2016 American Community Survey 1-Year Estimates, U.S. Census Bureau, 2015 American Community Survey 1-Year Estimates, 2014 American Community Survey 1-Year Estimates, 2013 American Community Survey, 2012 American Community Survey, 2011 American Community Survey, 2010 American Community Survey, 2009 American Community Survey 1-Year Estimates, 2008 American Community Survey, 2007 American Community Survey, 2006 American Community Survey and 2005 American Community Survey

**Figure 14: Tenure Distribution by Household Income (2011)**



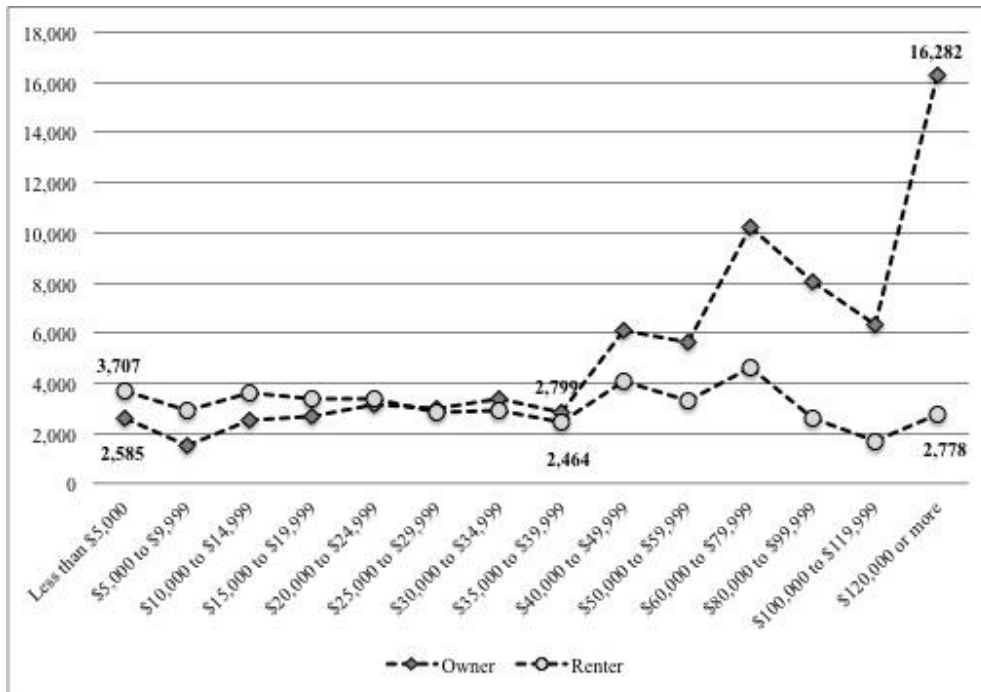
**Source:** U.S. Census Bureau, American Housing Survey. (Table of 2011 National - Income Characteristics - All Occupied Units, Variable 1: Household Income, Variable 2: Tenure generated on 03/04/18:14:22:34)

**Figure 15: Tenure Distribution by Household Income (2013)**



**Source:** U.S. Census Bureau, American Housing Survey. (Table of 2013 National - Income Characteristics - All Occupied Units, Variable 1: Household Income, Variable 2: Tenure generated on 03/04/18:14:24:42)

**Figure 16: Tenure Distribution by Household Income (2015)**



**Source:** U.S. Census Bureau, American Housing Survey. (Table of 2015 National - Income Characteristics - All Occupied Units, Variable 1: Household Income, Variable 2: Tenure generated on 03/04/18:14:25:29)

Thus the housing problem for renters (who are unable to easily switch to owning a home) can be summed up in terms of a growing gap between the cost of housing (including other associated costs such as utilities) and renter households' incomes. Marginal increases in this affordability gap tend to have a more negative impact on households that spend a larger proportion of their income on rent, which are typically the low or extremely low-income households.

Since the two main factors associated with the affordability gap, income and rent, are impacted by the business and housing cycle respectively, we can anticipate that as incomes fall during a downturn and prices (rents) remain sticky in the downward trend, that a growing proportion of low-income households (including those who may qualify for rental subsidies/assistance) will fall into the affordability gap when the business cycle contracts and moves into a recession as more households at the lower end of the income distribution switch from owning to renting homes. Given the trends seen in the most recent crisis indicate a 'jobless recovery' (Nikiforos 2013) and rising rents, another recession could worsen the affordability gap for low-income and very low-income households.

### **Federal Policies Used to Mitigate the Affordability Gap**

The two most prominent sources of direct government housing assistance to low-income households (renters) are rental vouchers (Section 8 and Housing Choice Vouchers<sup>4</sup>) and public housing. Low Income Housing Tax Credits (LIHTC), which are government tax subsidies that serve as an incentive to investors to invest in low-income housing, count as indirect government expenditures towards rental assistance (Fischer and Sard 2017). Of these two, the federal government favors the promotion of the former over the latter; in 2015 out of approximately \$56 Billion spending towards rental assistance, around \$30 Billion (roughly more than 50 percent) was spent on Section 8 voucher programs, while only \$5 Billion was spent on the maintenance and redevelopment of public housing (Fischer and Sard, 2017).

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<sup>4</sup> The Housing Choice voucher system constitutes the largest federal government assistance program for very low-income families (families earning 80 percent or less than their metropolitan or real area's median income- [ICPH] 2015, 103). Assistance extends to the elderly as well as the disabled. Under the program participants can use vouchers to find their own housing and is not necessary restricted to subsidized housing projects. The Housing Act of 1974 was established to offer the first national voucher program, known as the Section 8 Existing Housing Program (Schwartz 2006, 149-150).

This bias towards the use of voucher programs as the main source of rental assistance may exist for a variety of reasons; but a major one is certainly that, rental voucher programs enable affordable housing units that are produced by the private sector to be absorbed more efficiently by low-income households and thereby justifies the investment in low-income housing by the private sector. As a result, affordable housing remains a viable investment option to the extent that rising rents do not adversely affect demand.

Also, federal government tax subsidy programs as the LIHTC offer incentives to the private sector to invest in more affordable (low income) housing. While such incentives may not always result in an expansion of housing stock, they still constitute a much larger proportion of indirect rental assistance by the federal government than other forms of fiscal spending. A 2002 study of the LIHTC program and its effectiveness in increasing the supply of housing showed that it was not an effective incentive for the private sector to produce more low-income housing. The study concluded that there was no significant relationship between the number of units built through LIHTC and other subsidized units, in any given state and size of the existing housing stock (Malpezzi and Vandell 2002).

In addition, rental voucher programs (such as Section 8 and the Housing Choice Voucher program) are means-tested forms of government assistance and are only offered to qualifying households; i.e., households who earn 80 percent or less of the metropolitan or rural areas median income and spend 30 percent or more of their income on rent to qualify for assistance ([ICPH] 2015, 103). At first glance such programs would appear to be more cost-effective and timely solutions to addressing the affordability gap, but in a supply-restricted market the effectiveness of such policies is limited. If housing supplies could respond flexibly enough through the price mechanism in the short run, then rental vouchers would help to ensure that housing is distributed evenly enough among households across the income distribution.

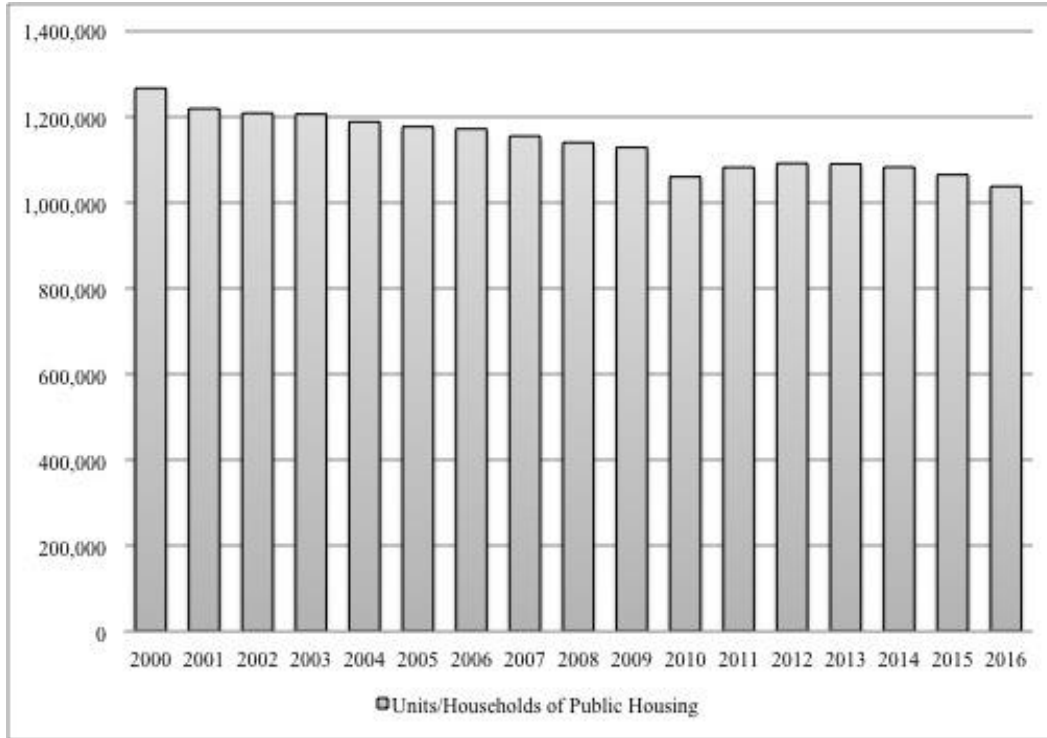
In fact, most low-income households do not receive the federal assistance they require; 75 percent of low-income renters do not receive federal rental assistance (O' Flaherty 2011; Fischer and Sard 2017). Even while rebounding, an economy may experience some proportion of its low income housing demand not being met directly as a result of inadequate rental assistance. This situation becomes a cause for serious concern in the event of a recession, when a much

higher proportion of low-income households will suddenly require assistance because not enough households who originally applied for assistance received the assistance they sought (O'Flaherty 2011).

Thus far we have seen that government incentives to boost investment in affordable housing via the private sector do not have the intended effect and that rental assistance provided by the government is not sufficient to meet the demand for affordable housing by sufficiently reducing the affordability gap. Furthermore, even the most dominant rental assistance programs currently offered cannot effectively cover the housing needs of low-income households in a supply restricted housing market. The only remaining viable option that can both mitigate the affordability gap and help reduce supply restrictiveness in the market is for the federal government to expand its provision of public housing to low-income households, but this approach is one that has been the least favored of governmental fiscal measures concerning housing. The national stock of public housing is being demolished at a faster rate than units are currently being replaced. Figure 17 below shows the total stock of public housing units for each year between 2000 and 2016, as reported in HUD's annual performance and accountability reports for those years. We can see that public housing stock dropped by around 200,000 units within that time period. The percent decline of public housing stock from the previous year is seen in the figure 18 below. The highest drop in public housing units occurred between 2009 and 2010, dropping almost 6.1 percent, indicating that government cut-backs on spending in the housing sector included the removal of units in an already supply restricted market.

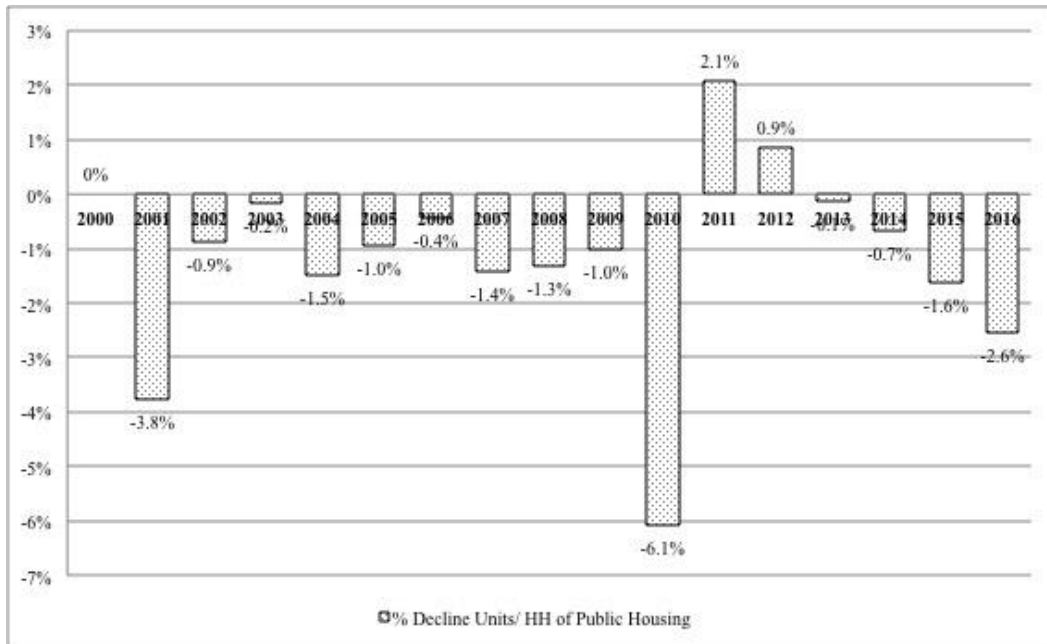


**Figure 17: Total Number of Public Housing Units (2000–16)**



**Sources:** HUD Performance and Accountability Report FY 2003, FY 2006 and FY 2009. HUD Annual Performance Report FY 2012, FY 2013 and FY 2016.

**Figure 18: Percentage Decline of Public Housing Units (2000–16)**



**Sources:** HUD Performance and Accountability Report FY 2003, FY 2006 and FY 2009. HUD Annual Performance Report FY 2012, FY 2013 and FY 2016.

The reduction in public housing stock has been taking place since the 1970s and has led to a chronic shortage in affordable housing. This shortage in affordable housing plays a role in explaining the relatively high level of homelessness we see today. The decline in supply of low-cost housing, especially among the very lowest-priced units, is the direct result of a decline in federal support for public housing construction, growing waiting lists for public housing, the fact that increasing home ownership costs leads to more frequent displacement, and abandonment of residential buildings and the widespread demolition of single room occupancy hotels that once served as a source of shelter to socio-economically displaced members of society. The empirical analysis conducted by Eliot and Krivo (1991) on whether or not low-income housing impacts homelessness, concluded that a mere 1 percent increase in the quantity of low rent housing would decrease the national homelessness rate by 2.2 percent, making it quite evident that a lack of low-rent housing is related to substantially greater levels of homelessness (Eliot and Krivo 1991)

While there are empirical studies such as the one conducted by Leung, Sarpca and Yilmaz (2012) that indicate that rental voucher programs lead to less distortion in social welfare than public housing and improve the overall level of social welfare by ensuring that housing voucher consumers have the option to move to neighborhoods with better schools and amenities, such studies are based on the primary assumption that the presence of public housing is the main reason the neighborhood where it is located incurs property tax losses. While historical property tax trends may indicate this to be true, the negative stigma attached to public housing can be attributed to the outcomes of the way in which the public housing program was first designed; it was set to prevent competition with the private housing market and to also meet strict budgetary restrictions imposed on it by Congress.

Public housing projects since the 1930s were required to employ adverse selection, often only choosing tenants that were extremely poor or highly impoverished instead of catering to low-income families, who were the original targets of the program. The programs were also poorly designed and constructed (to keep within the projects' restricted budgets), and located only within jurisdictions that applied to host such programs, which meant they were more often found to be disproportionately located in areas with a high density of low-income and minority neighborhoods, eventually making public housing programs emblematic of underdevelopment

and discouraged investment (Schwartz 2006, 105-8). Since the 70s public housing programs became less and less important as a share of fiscal expenditures.

The focus of federal housing policy measures still remains on mitigating the affordability gap experienced by low-income households through rental assistance rather than on the expansion of physical housing stock to meet the supply gap. This calls into question the effectiveness of such programs when the supply of affordable housing continues to decline. This decline in supply of low-cost units is the outcome of federal housing policy that is rooted purely in demand-side theory biased towards home-ownership, and the private housing market to ensure that the housing sector remains a basis for macroeconomic policies used to stimulate economic growth. This stance however creates a divergence between the two main reasons for which housing is consumed; housing that one owns serves both as a primary source of shelter (necessity good) as well as a form of investment (capital good) that yields returns only if its real value exceeds user costs. For those who are unable to access the financial capital required to own a home, they must resort to consuming housing in its primary capacity; as a source of stable and dependable shelter.

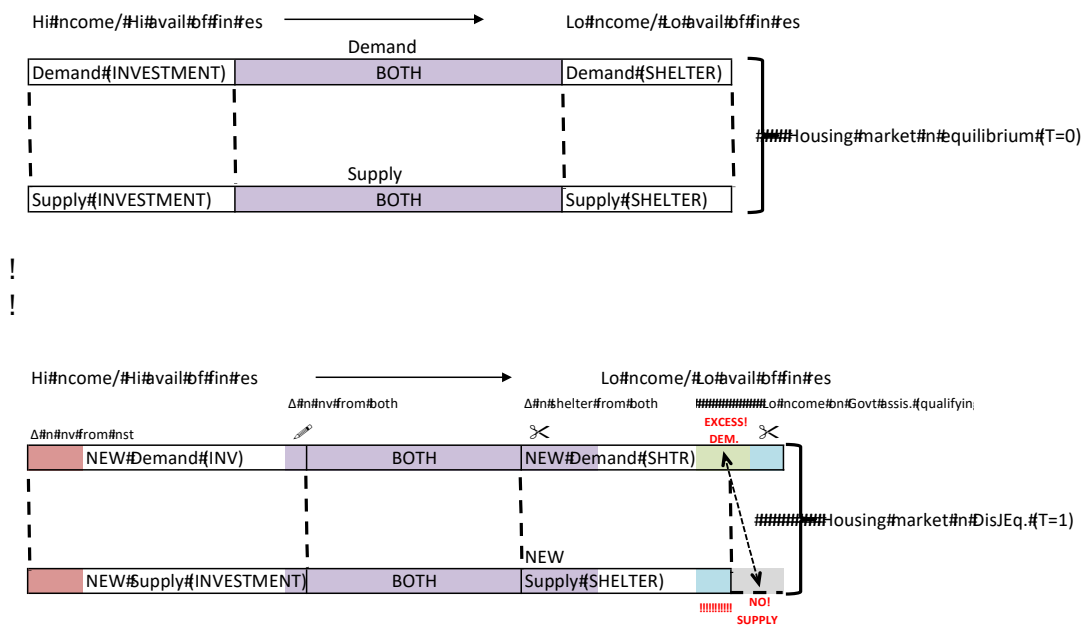
In an economy governed by federal policies structured to favor homeownership, the drive to consume housing for its dual benefits as a necessity good and a capital good would indefinitely be larger than that of consuming housing purely for the purpose of shelter (in other words renting). However, the choice between owning a home and renting a home is one that cannot be freely made as these are subject to constraints on affordability (mainly determined by income and the cost of homeownership) and the level of access households have to finance owning a home (either through savings or borrowing). The impact of these factors is a direct function of household income; households with high incomes tend to face a lower affordability constraint and access to credit than lower-income households.

The kind of housing that tends to be consumed varies in a similar manner across the income distribution of households; lower-income households with higher constraints on affordability and access to credit facilities tend to rent more, while higher income households have the option to do either, depending on which of the two constraints makes them better off. In an environment where the user costs of homeownership are rising, more high-income households

will switch to renting their primary form of shelter by using their savings and borrowing to finance their investment. This would be unproblematic if the market-clearing mechanism somehow enabled low-income renters to rent the surplus of new housing stock that remains unsold in such a situation, but unfortunately this is not how the housing sector works. The vacant lots remain vacant until the market picks up again and with the rising number of high-income households who shift to renting, there is a relatively higher proportion of renters in the aggregate economy who can absorb higher rents and cause the displacement of low-income renter households who are more susceptible to rising rents and become ‘crowded out’ of a supply-constrained market.

To visualize how such displacement occurs, let us consider the following scenario of an economy whose housing sector is in equilibrium (at time  $T=0$ ) and then experiences a demand shock in the form a decrease in the short term nominal interest that spurs an increase in the demand for single family units at time  $T=1$ .

**Figure 19: Conceptual Framework of Mismatch between Housing and Homelessness Policy**



Source: Author’s own calculations

In the figure above the demand for total housing units is split into a demand for housing purely as capital goods for investment on the extreme left (these would typically be demanded by institutional investors who seek to sell or rent these units to other market participants (mainly households)) to households that demand housing both for shelter and investment in the middle (households who choose to own their primary source of shelter rather than to rent) and to households that demand housing purely as a form of shelter (households who have no choice but to rent given their constraints on affordability and access to credit) on the extreme right hand side.

High-income/high-net-worth households that have a higher capacity to access mortgage lending by banks (facilitated by federal policy that creates market conditions favorable to homeowners) or have a higher level of savings/endowments that enable them to move freely between homeownership or renting their primary source of shelter, are represented on the left of the diagram. Lower-income/lower-net-worth households who possess a diminishing capacity to access mortgage finance and possess little or no savings/endowments and therefore cannot move freely between decisions to own or rent their primary source of shelter are represented on the right. The latter group must choose to rent if they are to remain sheltered and tend to be more susceptible to factors that impact the affordability gap as described earlier.

Let us assume for simplicity's sake that at  $T=0$  that supply and demand for housing are in equilibrium and that the market for investment and shelter both clear. At  $T=1$ , due to a decrease in the nominal short-term interest rate and anticipated increases in the future prices of single family units, institutional investors and households that face lower income and borrowing restrictions begin to demand more single family units, the increase in demand is most quickly reflected on the left-most section of the demand spectrum which is highlighted in pink (within the sector of the economy that can make and execute investment decisions most flexibly due to macro policy that works in their favor).

In the short term, households that initially demanded housing both for investment and as shelter and who are closer to the higher income end of the income distribution (closer to the left hand side than the right) can flexibly shift from owning just one unit to multiple units, and those closer to the middle may be able to shift from owning a smaller unit to a larger one (trading up).

A larger proportion of those households that have to rent may now demand more rental units instead of trading up or making home purchases as rents initially appear lower due to the drop in user cost at  $T=1$  (this effect tends to be more dominant in urban areas where the value of housing is much higher than suburban areas, thereby making short-term adjustments from renting to homeownership difficult).

When the economy begins to expand (and interest rates are low) better job prospects and rising incomes will cause average household size to drop and the number of households to expand putting upward pressure on the number of units demanded for shelter (rental) in highly urbanized areas. Of course the sticky short-run supply leads to a mismatch between those who can only consume housing for shelter (renters) even if they qualify for means-tested housing assistance (green section) and the total number of rental housing units available (vacant units for sale are excluded from the supply of housing renters have access to unless they are somehow made available to them for rent).

What is surprising is that it is not households on the extreme right (the poorest households), who have access to physical housing units provided by the government (even if poorly maintained) in the form of physical public housing units (blue), that end up being displaced, but the low and extremely low-income households who are above them on the income distribution. The gap in supply needed to enable the market to reach equilibrium in time period  $T=1$  is shown in gray; this is the portion of housing supply (mainly low-income housing) that falls into the disequilibrium gap; large institutional investors seeking to maximize their profits would not be willing to undertake investments that will not appreciate much in value or that cannot be afforded by low-income households due to their susceptibility to the affordability gap and this widens the supply gap. Similarly the decline in government expenditure on public housing will also tend to widen the gap in the supply of housing stock.

Subsequently when economic expansion leads to higher inflation and tighter monetary policy, the increase in user cost makes investment in housing less profitable but, as seen earlier, rents and housing prices will be slow to adjust downwards even with a reduction in investment (supply) of new units. At the same time, the effects of high economic growth and high inflation would have led to rising unemployment (income shock), resulting in a further increase in the

demand for affordable rental units amongst low-income households (because of excessively high rents due to rising user costs), widening the gap between demand and supply even further. Ultimately those who cannot access the housing they need are those who will face worsening affordability issues in an already supply-restricted housing market; these households remain on the verge of being made homeless as a result of policy failure rather than personal circumstances.

## **VI. WHO ARE THE IMMINENTLY HOMELESS?**

Dolbeare (1992) shows that the affordability gap is the principal underlying cause of homelessness in the 21 century. While homelessness is not a new phenomenon, by far, the studies associated with its analysis began in the 1980s in the United States, among social theorists, when homelessness first became a more conspicuous social phenomenon. These theorists discovered that the reason behind the increasing visibility of the homeless was the large-scale elimination of their existing sources of shelter: single row homes or skid row-type accommodation that were cleared to make way for urban revitalization and development programs. Prior to this era of urban revitalization most homeless individuals were capable of maintaining some form of employment and retaining some form of protective shelter, even if not under the most ideal of living conditions.

The body of knowledge surrounding homelessness and our understanding of it does not extend far beyond empirical studies that estimate the size of the homeless population or descriptive studies of the demographic and personal characteristics of the homeless that includes their living conditions (Elliot and Krivo 1991). While the structural causes of homelessness can be attributed to high poverty rates, poor economic conditions and personal circumstances that are not supported by adequate mental health care facilities, it is the lack of affordable housing or more so the affordability gap that is often cited as the main cause for homelessness (Elliot and Krivo 1991; Dolbeare 1992; O' Flaherty 2009 and [ICPH] 2015).

In the United States, HUD measures homelessness rates through administering its annual “Point in Time” (PIT) counts. These are simply headcount measures of the visibly homeless that enable HUD to keep track of their numbers according to certain demographics like age and family status. Reports on PIT counts have been issued annually since 2007 and form an important aspect of HUD’s Annual Homelessness Assessment Report to Congress (AHAR).

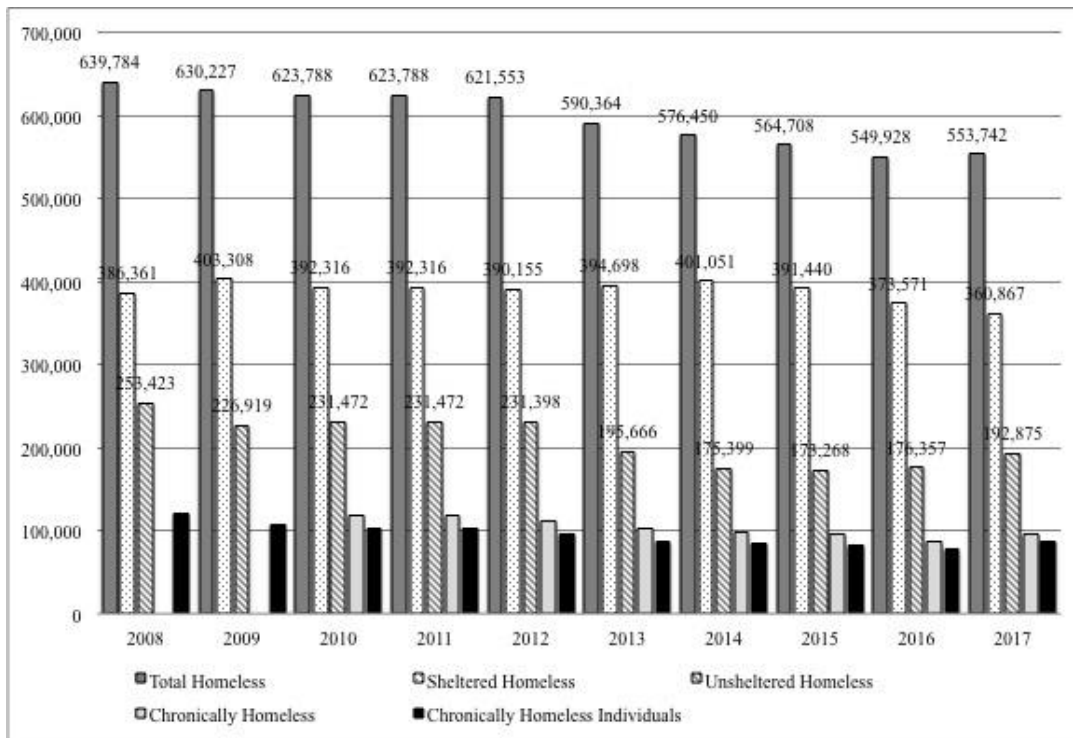
Unfortunately, there is no examination of the causes or reasons for homelessness reflected in PIT counts. Nonetheless, this forms the closest record of the homeless that can be used to assess trends in homelessness rates/numbers. Figure 20 below shows the PIT counts of the total number of homeless in the United States between 2008 and 2017, divided into different categories identified by HUD.<sup>5</sup> The chronically and unsheltered homeless constitute smaller proportions of the total number of homeless when compared to the sheltered homeless. It appears that those who are predisposed to imminent homelessness would fall within the category of either the sheltered or unsheltered homeless, depending on whether or not they qualify/have access to homeless shelter facilities.

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<sup>5</sup> “Chronically Homeless Individual refers to an individual with a disability who has been continuously homeless for one year or more or has experienced at least four episodes of homelessness in the last three years where the combined length of time homeless in those occasions is at least 12 months. Sheltered Homelessness refers to people who are staying in emergency shelters, transitional housing programs, or safe havens. Unsheltered Homelessness refers to people whose primary nighttime location is a public or private place not designated for, or ordinarily used as, a regular sleeping accommodation for people (for example, the streets, vehicles, or parks).” (Department of Housing and Urban Development 2017, 2)



**Figure 20: Point in Time Counts (2008–17)**



**Source:** Department of Housing and Urban Development Point-in-Time (PIT) estimates (2007-2017) (<https://www.hudexchange.info/resource/3031/pit-and-hic-data-since-2007/>)

The federal assistance provided to the homeless is captured in their homelessness inventory counts, the number beds at shelters and other units of supportive and temporary housing that ensure that the homeless are at least, for a limited time, not exposed to the detrimental effects of being openly homeless. Figure 21 below shows the total number of beds that can be accessed year-round at shelters, between 2010 and 2017. During this period we can observe that there are enough resources to cover the number of openly homeless individuals or households that are counted in PIT estimates, yet unsheltered homelessness tends to persist. The reason for this could most likely be a system of means testing within homelessness shelter programs that limits the access to such shelters to only a fraction of those who are openly homeless.

**Figure 21: Trends in National Homelessness and Total Year-Round Beds at Shelters (2010–17)**

Year	Total Year-Round Beds (Across All Programs)	Total Homeless Count	Bed/Homeless Count Ratio	Homeless Count/Annual Population Estimate Ratio
2010	661,230	623,788	1.06	0.20%
2011	696,941	623,788	1.12	0.20%
2012	703,313	621,553	1.13	0.20%
2013	730,376	590,364	1.24	0.19%
2014	772,788	576,450	1.34	0.18%
2015	829,581	564,708	1.47	0.18%
2016	867,102	549,928	1.58	0.17%
2017	899,059	553,742	1.62	0.17%

**Source:** Department of Housing and Urban Development Housing Inventory Count (HIC) data (2010-17)  
(<https://www.hudexchange.info/resource/3031/pit-and-hic-data-since-2007/>)

**Figure 22: Trends in Homelessness and Total Year-Round Beds at Shelters in New York State (2010–17)**

Year	Total Year-Round Beds (Across All Programs) NY	Total Homeless Count NY	Bed/Homeless Count Ratio	% of Total YR Beds	% of Total Homeless Count	% Change in Homeless Count from Prev. Year	Homeless Count/Annual Population Estimate Ratio (NY)
2010	99,355	65,606	1.51	15%	11%	N/A	0.34%
2011	103,665	63,445	1.63	15%	10%	-3.3%	0.32%
2012	99,492	69,566	1.43	14%	11%	9.6%	0.35%
2013	108,274	77,430	1.40	15%	13%	11.3%	0.39%
2014	114,667	80,590	1.42	15%	14%	4.1%	0.41%
2015	130,206	88,250	1.48	16%	16%	9.5%	0.45%
2016	130,049	86,352	1.51	15%	16%	-2.2%	0.44%
2017	135,102	89,503	1.51	15%	16%	3.6%	0.45%

**Source:** Department of Housing and Urban Development Housing Inventory Count (HIC) data (2010-17)  
(<https://www.hudexchange.info/resource/3031/pit-and-hic-data-since-2007/>)

Figure 22 above shows the number of year-round beds available and the total count of the homeless in the State of New York between 2010 and 2017. On average the number of beds in the state constitutes around 15 percent of the total number of year-round beds available, while the homeless in New York comprised on average 13 percent of the total homeless population within that time period. The ratio of the homeless count to total population estimates for each year between 2010 and 2017 as shown in each of the tables above, shows that New York experiences a higher rate of homelessness than the national average, indicating that homelessness is generally more prevalent there than across the rest of the country, even with sufficient shelter made available to the homeless at any point in time. In fact, in New York homelessness appears to be increasing while it appears to be declining at a national level since 2010. Therefore even though the support offered through shelter-based programs is necessary in mitigating homelessness (Goodman, Messeri and O’ Flaherty 2016), it does so only to a certain

extent and is not a sufficient solution to reduce homelessness in the long run, especially in areas like New York where homelessness has been a systemic problem for many decades.

Homelessness measures and the programs in place to assist them are not structured with the purpose of proactively reducing their numbers in future. Had this been the aim, there would be more efforts undertaken to understand the nature of what precipitates homelessness, especially the economically related factors. This deficiency in policy and program structure directly impacts a subset of the homeless that are overlooked by academic research; the imminently homeless.

“Near” or imminent homelessness is different from HUD’s definition of the sheltered homeless, which has a specific definition in HUD’s Annual Homelessness Assessment Reports (AHAR); the AHAR consistently refers to the ‘sheltered homeless’ as “people who are staying in emergency shelters, transitional housing programs, or safe havens” (Department of Housing and Urban Development 2017). In January 2012, HUD published an independent two-page document that reviews the definitions of the constituents of homelessness and the associated record-keeping requirements in line with each. The memo identified individuals or families as “imminently at risk of homelessness” if:

“...the individual or family who will imminently lose their primary nighttime residence, provided that: (i) Residence will be lost within 14 days of the date of application for homeless assistance; (ii) No subsequent residence has been identified; and (iii) The individual or family lacks the resources or support networks needed to obtain other permanent housing (Department of Housing and Urban Development 2012).”

The above requirements stipulate that there is some record of the number of imminently homeless that HUD generates but does not introduce in any of its publications. It can be surmised that the lack of data on the imminently homeless is impeding further academic research on this phenomenon.

There are however a few examples of stand-alone surveys of aspects that relate to imminent homelessness. One feature of the imminently homeless is that they often ‘double up’ in an effort

to remain housed. Doubling up refers to the process of individuals or groups of individuals moving into or out of related or unrelated households. The 2013 American Housing Survey (AHS) included a national summary table that summarized statistical data from the survey for that year. It included a special supplemental report on the number of “Doubled Up Households — Movers Leaving and Entering Unit”— a record that has neither been included in their subsequent housing survey of 2015 nor included in the summary tables for the previous survey in 2011. Further details of the survey questions and responses presented in this report are included in the appendix.

Another example of a more thorough one-off survey used to identify the type of shocks that are likely to precipitate homelessness is the 1992 report of the New York City Commission on Homelessness (O’ Flaherty 2009, 3). The survey is based on open-ended questions posed to the residents of city shelters. The response to one question is of particular importance here: “What would you say is the main reason you became homeless?” Out of 485 respondents from family shelters, 21 percent cited a lack of ability to pay rent as a primary reason for why they became homeless, housing being too crowded followed at 12 percent and a lack of employment was third at 9 percent. Among 487 respondents from single shelters, approximately 27 percent listed lack of employment as a primary reason for being made homeless, while 28 percent cited drugs and alcohol and 11 percent due to the inability to pay rent. The remaining reasons were welfare problems, illness/injury, jail/arrest, relocation, eviction, fire, unsafe housing and other social reasons had the response rates for these categories ranged between zero to nine percent for both single and family shelter respondents (O’ Flaherty 2009, 3). A similar survey is not known to have been subsequently produced, and which might serve as a better indicator of changes in factors that affect those who are imminently homeless, and the results of which might be useful in drafting remedial policies and programs targeting the long-term reduction of homelessness in the United States.

### **How the Mismatch Between Federal Housing and Homelessness Programs Impacts the Imminently Homeless**

In chapter V we reviewed the possible implications of continuing to implement federal housing policies with a demand-side bias on an asymmetric housing market. The continual mismatch between the effective demand for and supply of housing is exacerbated under policies structured

to favor the demand for housing as an investment good, when in fact housing, whether bought or rented, primarily serves as a source of stable shelter. On one hand, housing policies omit the importance of housing as stable shelter, resulting in the failing of some people to access adequate and stable shelter from time to time, while on the other hand homelessness programs offer shelter with no guarantee of stability, generating a mismatch between policy objectives that should have concurrent objectives.

The mismatch between these two policy sides is problematic in the long run; the weaknesses in federal housing policy contributing to the demand supply gap leads to a higher level of government spending on homelessness programs in the long run. This in itself appears to be counterintuitive to the aim of housing policy as espoused in the Housing Act of 1949, wherein access to adequate shelter is a promise made to every American irrespective of their representative level of household income or their preferences relating to the kind of housing they choose to dwell in.

The most prominent examples of the failure of housing policy to meet its promise are associated with policies that were intended to ensure that low-income households received better access to adequate housing. The three different low-income housing programs that are critiqued in this section are: privately owned subsidized housing, low income Housing Tax Credit (LIHTC) backed housing, and Housing Choice Voucher programs. While each program is structured with different objectives, their implicit starting-point remains the same, to promote the growth of the housing sector.

Privately owned subsidized housing programs emerged in the 60s and 70s in response to increasing criticism of public housing programs. They were established to serve households with incomes that were too high to qualify for public housing, but too low to afford housing within the private sector. Public- private partnerships would agree to construct or provide housing which was then offered at reduced rents to low-income households for a specified number of years in exchange for securing better-than-market rates of financing (thereby making it profitable for them to invest in the development of more affordable housing projects). Rental subsidies were incorporated only later into such programs; the initial approach to ensuring that low and moderate income households could participate in them was to limit construction costs

as much as possible (Collinson, Ellen and Ludwig 2015). While limiting costs makes sound investment sense, the lowering of construction costs, more often than not, requires the utilization of cheap quality materials. This implies that the quality of housing provided to low and moderate income households under such projects is likely to substandard and that housing units offered by the program may incur a higher level of future repair costs that may be passed on to participants of the program.

Herein lies the problem of driving macro-dynamic growth using the housing sector; growth is stimulated within the construction and construction-related sectors, and as the targeted level of growth is achieved in these sectors; they will most likely be the first to face inflation. Thus construction costs, irrespective of whether they are associated with low-income housing projects or otherwise, tend to rise rapidly as the housing cycle moves upwards. Homes constructed towards the peak of the housing cycle tend to be relatively more expensive than those completed earlier on when costs were lower. The rise in costs necessitates the charging of higher rents on newer homes, thereby rendering rental subsidies under the program ineffective in reducing rents to an affordable level for participants, especially those who fall within the lower income brackets. This pricing out of low-income households replaces them with moderate-income households as the major consumers of privately owned subsidized housing. To ensure better affordability by low-income participants in the program, spending on federal rental subsidies had to increase. With time, spending levels on rental subsidies were deemed excessive and by 1983, the program was cut back drastically and replaced with Low Income Housing Tax Credits (LIHTCs), under the Tax Reforms Act of 1986 and Housing Choice Voucher programs.

LIHTC- backed housing is offered mostly on a flat-rent basis and is normally independent of a tenant's income. Flat rents on LIHTC program housing cannot be set at a level higher than what is considered affordable according to a qualifying household's maximum income. Thus developers can charge rent that is below this ceiling but may still be high in relation to the household's income, causing some households to pay a much larger share of their income on rent than HUD's 30 percent threshold for affordable housing. On the other hand, households living in LIHTC developments are not subject to scrutiny of changes in their incomes, implying that they are not required to move out even if their incomes rise to the point that their rent burdens fall well below 30 percent of income. In an environment where housing in general

remains in short supply, the use of flat-rents dampens the revenue generation prospects of LIHTC investors, which puts further downward pressure on the supply of affordable housing. The short supply of LIHTC housing is further worsened by units rented by household with increasing incomes not being vacated enough to accommodate newer households with lower incomes and higher rent burdens (Collinson, Ellen and Ludwig 2015 and Freeman 2002, 710).

There are a variety of housing (rental assistance) programs, but all are based on the principle that tenants facing rents above 30 percent of their income can avail themselves of federal assistance that covers the difference, but only up to a specified maximum remuneration standard (Collinson, Ellen and Ludwig 2015). These standards stipulate that in the first year of the program, tenants should pay no more than 40 percent of their income on rent but that in subsequent years this threshold can increase. Housing Choice Voucher programs require an annual recertification of income of voucher holders and is means tested to ensure that support is offered only for housing units meeting a minimum quality and size standards. While Housing Choice Voucher programs now constitute the largest housing subsidy to low-income households, thereby highlighting their popularity as a federal initiative, such programs can only improve the affordability of housing where there is adequate supply. The only way in which the Housing Choice Voucher programs can be made more successful in their role of improving housing affordability is by increasing the supply of affordable housing, because the former has no use in the absence of the latter.

It is clear now that the structures of some of the most prominent housing programs in use today have the potential to aggravate homelessness, when households that are not fully supported under such programs face rental or income shocks and become imminently homeless. Currently the homeless are collectively supported by federal homelessness programs only to the extent of mitigating their immediate need for shelter. Homelessness policies need to emphasize a more proactive approach towards the reduction of homelessness. The policy change accompanying such a proactive approach would require an understanding of why the homeless become homeless in the first place. An example pointed out in Goodman, Messeri and O'Flaherty's 2016 paper on the effectiveness of homelessness prevention programs in New York City is that of the 'Homebase' program that supports homeless families by helping them access homeless shelters. As, the program itself was only designed to help families overcome their 'immediate

housing problem' (Goodman, Messeri and O'Flaherty 2016) it misses out on the opportunity to understand what gets them into the shelter in the first place. Once the causal factors for homelessness are established they need to be differentiated into ones based on economic conditions and non-economic conditions, because the former is best suited to preventative measures while the latter is not.

The shelter-based approach is still the best solution to counteracting the immediate effects of homelessness, thereby making it a relatively successful solution for the chronically homeless who are more often found to be so due to non-economic related conditions, such as substance abuse problems or mental health issues. Whereas homelessness caused by non-economic factors can only be mitigated, homelessness caused by economic conditions can be prevented by making better efforts to monitor and identify the imminently homeless (Goodman, Messeri and O'Flaherty 2016) and developing supportive policies that prevent the imminently homeless from becoming homeless. Local and federal housing and homeless policies must work together to ensure that homelessness arising from economic conditions is completely eliminated.

### **What is an Alternative Approach?**

Scholars who attempt to study the links between welfare policies and homelessness generally follow a dual hypothesis: 1) countries with a lower level of poverty and inequality and larger welfare systems tend to have a lower level of homelessness than those with higher levels of poverty and inequality and smaller welfare systems, and 2) homelessness in countries with larger and more extensive welfare systems is more likely to be concentrated amongst individuals with 'complex support' needs (e.g., mental illness or substance abuse) rather than those with smaller and less extensive welfare systems where homelessness is more likely to occur as a result of poverty and housing affordability problems (Benjaminsen and Andrade, 2015). They posit that in a liberal welfare system such as that of the United States, a combination of high levels of both poverty and income inequality, a lack of social housing schemes, and a relatively weak welfare system all contribute to rising levels of homelessness represented more broadly by the poor population and those that are homeless due to non-economic personal conditions. They arrive at this conclusion by comparing the US welfare system with the social democratic welfare system of Denmark; a country which they point out has lower levels of poverty, a much larger



public housing sector and an extensive welfare system, where homelessness is precipitated more by noneconomic conditions rather than economic ones.

The financialization of homeownership and housing rights was an ode to late neoliberalism, which when combined with the dismantling of housing welfare through the privatization of public housing initiatives, large-scale reductions in public housing investment and other welfare programs since the 80s in the US, turned housing into an investment asset rather than a human right (Rolnik 2013). The excessive commodification of housing, often abetted by government policies biased towards this outcome, has had disastrous effects in the recent past that are only likely to be worse in the event of future income and housing price shocks, and leaving those who are unable to exercise their right to shelter to become the most adversely impacted. Therefore it seems apt that the path to reformative housing policy should begin with addressing housing as a basic human right, that is, as a fundamental need rather than a want. The recognition of the right to adequate housing as a basic human right is increasingly being reflected in international law. The United Nations' Committee on Economic Social and Cultural Rights (CESC) stipulates that: "...the rights to housing not be interpreted in a narrow or restrictive sense which equates it with, for example, the shelter provided by merely having a roof over one's head or views shelter exclusively as a commodity. Rather it should be seen as the right to live somewhere in security, peace and dignity." (Andrews et al. 2016, 2) Likewise the Universal Declaration of Human Rights asserts, "...everyone has the right to a standard of living adequate for health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services." (Andrews et al. 2016, 3). These inclusions are founded on the basis that the inability to observe one's right to access the bare minimum level of housing impedes the individual right to life, liberty and security of person (Andrews et al. 2016,7).

The system of housing and homelessness related policies as examined thus far, attempts in various ways to provide housing to those most in need, especially families with children and veterans. However it is yet to integrate a fundamental principle of housing being a human right to its policy changes. In fact a true right to housing has never been recognized in federal housing policy at all, and as a result 'discrimination in housing persists' (Andrews et al. 2016, 13 and Byrne and Culhane, 2011). Future remedial measures in housing and homelessness prevention

policies must take into consideration the basic human right to housing; without it, the effects of economic uncertainty lead to untenable and stigma-generating outcomes for those affected, that inhibits them from living at their full social and economic potential (Byrne and Culhane 2011, 381)

The 'Housing First' model is an existing policy framework, which embodies the principle of access to housing as a basic human right. In the United States the Housing First model has gained recognition mostly through pioneering work conducted by 'Pathways to Housing'. The Pathways to Housing website (Pathways Housing First 2018) identifies it as a non-profit agency established in 1992 that advocates for the direct provision of housing as a primary solution to homelessness amongst those who are mentally ill or have no alternative option for remaining permanently housed (Atherton and Nicholls, 2008). The key characteristics of the Housing First model include the offer of stable housing with no pre-conditions to be satisfied by those who avail themselves of its benefits, such as a commitment to sobriety. The offer of housing is accompanied by supplementary supportive care programs to help tenants who seek to improve their physical and social condition, but their acceptance is by no means enforced as a condition for retaining housing benefits; at no time are tenants under the threat of eviction because of their personal condition or circumstances and involves the direct combination of providing stable shelter without a means-tested approach.

This stands in direct contrast with the Continuum of Care (CoC) approach followed by HUD's homelessness-reduction policies and programs. The CoC approach works on a system of advancement from one step to the next by homeless individuals or families towards the achievement of stable housing. The CoC approach also enforces abstinence from socially and personally destructive behavior (Atherton and Nicholls 2008) as part of its requirements for accessing housing assistance.

The exclusion of the need for pre-conditions to be satisfied under the Housing First model makes it an apt solution for mitigating homelessness amongst those with non-economic conditions, especially when it has proven to be a more economical solution to homelessness than the current shelter-based ones (Atherton and Nicholls 2008). The question that arises at this juncture, given the acceptance of housing as a basic human right, is whether or not this model of

homelessness reduction should be extended to cover those who are rendered homeless as a result of economic conditions related to the housing market as seen earlier. The explicit ‘social contract’ embodied in the promise of the 1949 Housing Act implies that this approach would not be misplaced; as specified in the Act there must be “a realization as soon as feasible of the goal of a decent home and suitable living environment for every American family” (Freeman 2011, 709). While the offer of housing alone does not solve the problems leading to homelessness, the Housing First model would be an apt way to formulate a basis for government intervention in mitigating the supply-glut that ultimately contributes to homelessness. Expansion of the government’s public housing stock, through the construction of new units, conversion of government fixed assets to housing stock or acquisition of housing units from the private sector would collectively form the pool of housing for the economically disadvantaged who have no feasible options for housing left to choose from in the private sector, and thereby enabling the to exercise more equally the basic human right to housing.

## **VII. CONCLUSION**

Edith Elmer Wood was a housing reformer under the New Deal administration who advocated for adequate and affordable housing. Her 1934 paper titled: “A Century of the Housing Problem” echoes the chronic nature of housing inadequacy in the United States and how it most severely impacts the poor. She posited that the housing problem in advanced capitalist societies is not a problem that can ‘solve itself’ in the manner that free-market neoclassical general equilibrium theory explains. Demand-side biased federal housing policies first introduced by the New Deal Administration, generated inefficiencies in a market with the pre-existing tendency to remain in disequilibrium, and this can lead to a temporary exclusion of some proportion of households in an economy from accessing housing that is adequate and affordable. Federal housing policies are structured in a manner that facilitate the commodification of housing and its conversion to an investment asset rather than a basic human right, while only providing support to households that participate in their housing assistance programs to enhance their ability to afford market rents and housing values, an approach that is not sufficiently effective to prevent their inability to obtain affordable housing when faced with rental or income shocks. The bias towards demand-side policies that are focused on homeownership remains a fundamental

feature of housing policy in the US, as policymakers often look upon the housing sector as a macro-stabilizer that requires only a conservative level of fiscal expenditure to function successfully. However under such policies the housing market generates price increases that tend to be ‘sticky’ in the downward direction, making affordable housing less accessible. Rental assistance through housing voucher schemes target the reduction of the rent burden on low-income households, while tax credits under the Low Income Housing Tax Credit (LIHTC) program incentivize the investment in low-income housing through tax credits and cheaper financing, ultimately enabling more affordable housing to be produced for low-income households. However, the levels of government spending on rental assistance and other housing-assistance programs have been dwindling, while LIHTC has proven to be a not good enough incentive for investment in affordable housing. Housing policies focused on improving affordability in a supply-constrained housing market are ineffective in ensuring an equitable distribution of housing occurs across all households. The most efficient solution to ensuring that the effective demand for housing is met would be to increase government spending on the replacement and enhancement of public housing so as to increase the overall stock of affordable housing in the market, while acknowledging that out of the dual nature that housing serves as an investment good and as a necessity, its role as a source of shelter should be the primary focus of government housing policy.

The repercussions of not addressing the supply glut in affordable housing include homelessness. For those who face bouts of temporary homelessness as a result of economic conditions, the policy system in place offers the same generic level of support afforded to the homeless in general, which is simply to meet their immediate need for shelter. Thus, those who become homeless as a result of their inability to afford stable shelter are offered only a palliative solution to a recurrent problem. An evolution in homelessness policy, from focusing on homelessness mitigation to homelessness prevention, needs to take place, with better methods and systems in place to monitor the economic conditions that become the precursor to imminent homelessness. Such a change in homelessness policy would help prevent the imminently homeless from moving into a state of transient homelessness. While the term transience implies that there is an eventual turnaround in the state of homelessness that such households encounter, often such disruption leads to economic losses in the form of higher welfare spending on homelessness programs. The ‘savings’ from cutting back on the investment in the national

public housing stock since the 1970s (Foscarinas, 1990) eventually will manifest as higher long-term costs on the welfare spending needed to resolve an escalation of homelessness. One potential policy framework that future remedial housing and homelessness prevention policies can follow jointly is the Housing First approach, a model already in use as a non-means tested solution to homelessness reduction amongst those with mental illness or substance abuse problems. The same approach, in combination with an enhanced public housing stock, is suggested as a possible solution to ensure homelessness generated by economic conditions is reduced, until sufficient changes within homelessness policy measures are developed to monitor the factors contributing to imminent homelessness so as to prevent them from transitioning into a state of homelessness.

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## APPENDIX

### 2013 American Housing Survey: “Doubled Up Households — Movers Leaving Unit”

Characteristics	Total occupied units	Tenure		Housing unit characteristics		Household characteristics			
		Owner	Renter	New construction past 4 years	Manufactured/mobile homes	Black alone	Hispanic	Elderly (65 years and over)	Below poverty level
HOUSEHOLD MEMBER MOVED OUT OF UNIT IN PAST YEAR <sup>1</sup>									
Total	4,421	2,931	1,490	66	336	479	630	548	729
How Many Moved Out									
1 person	3,557	2,372	1,185	60	246	357	461	454	588
2 persons	537	368	169	3	35	73	113	75	92
3 persons	202	108	94	3	42	29	36	11	28
4 persons or more	126	83	43	—	13	20	20	7	22
Reason for Stay <sup>2</sup>									
Stayed due to lack of money or financial support	1,191	830	362	2	102	148	196	206	188
Did not stay due to lack of money or financial support	3,200	2,087	1,113	64	234	328	427	339	537
Not reported	30	14	16	—	—	3	7	2	5
Length of Stay <sup>2</sup>									
Less than 2 weeks	71	47	24	4	7	12	9	17	23
2 to 4 weeks	141	76	65	—	7	16	18	17	30
1 to 3 months	497	263	234	11	35	54	74	41	116
4 to 6 months	515	310	205	19	62	74	71	70	95
7 to 12 months	683	381	302	8	42	73	114	79	132
Greater than 12 months	2,506	1,851	654	25	185	250	340	324	332
Not reported	8	2	6	—	—	—	4	—	1
Forced to Leave <sup>2</sup>									
Asked to leave	320	203	117	9	30	29	39	33	89
Left voluntarily	3,422	2,255	1,167	41	251	377	538	380	530
Left for some other reason	667	461	206	16	54	72	53	134	111
Not reported	13	12	1	—	—	—	1	1	—
Reason for Leaving <sup>2</sup>									
Financial reasons	543	355	188	5	46	97	106	60	95
Crowding, conflict, or violence	250	140	110	—	24	14	53	32	70
A major change in family	1,279	891	387	30	117	105	183	114	235
Health reasons	222	164	59	3	24	18	26	96	48
To be closer to work or job	322	227	95	1	14	34	22	47	29
School or military	433	320	113	18	2	47	33	42	48
To establish own household	429	289	140	3	28	53	53	34	64
Other	900	524	376	7	81	110	146	118	134
Not reported	42	21	21	—	—	—	7	3	7
Where Moved <sup>2</sup>									
Own place	2,619	1,860	759	21	162	271	354	289	382
Home of relatives/friends	1,084	604	480	27	110	125	191	98	215
Dormitories or barracks	165	114	51	7	6	12	13	17	13
Foster care	11	7	4	—	—	4	—	4	7
Treatment program, hospital, or nursing home	67	53	14	—	10	7	5	33	19
Jail or prison	17	8	9	—	3	—	3	6	5
Shelter or other homeless program	12	10	3	—	4	—	6	1	—
Place not meant for habitation <sup>3</sup>	1	1	—	—	—	1	—	1	—
Other	306	202	103	3	29	44	14	85	56
Not reported	139	71	67	8	11	16	44	15	32

**Source:** United States Census Bureau, 2013 American Housing Survey for the United States

## 2013 American Housing Survey: “Doubled Up Households — Movers Entering Unit”

Characteristics	Total occupied units	Tenure		Housing unit characteristics		Household characteristics			
		Owner	Renter	New construction past 4 years	Manufactured/mobile homes	Black alone	Hispanic	Elderly (65 years and over)	Below poverty level
HOUSEHOLD MEMBER MOVED INTO UNIT IN PAST YEAR <sup>1</sup>									
Total	19,953	6,001	13,952	882	1,045	3,224	3,241	1,607	4,482
Reason for Stay <sup>2</sup>									
Staying due to lack of money or financial support	2,434	647	1,787	16	183	521	510	239	1,020
Not staying due to lack of money or financial support	17,263	5,254	12,008	859	856	2,656	2,707	1,322	3,405
Not reported	256	100	156	7	6	47	24	46	57
Forced to Leave Previous Residence <sup>2</sup>									
Asked to leave	922	199	723	26	61	129	184	94	319
Left voluntarily	16,511	5,035	11,476	783	819	2,651	2,675	1,237	3,534
Left for some other reason	2,262	660	1,602	63	159	395	356	228	579
Not reported	259	107	152	10	6	50	26	48	51
Reason for Leaving Previous Residence <sup>2</sup>									
Financial reasons	3,767	923	2,844	100	255	711	723	261	1,060
Crowding, conflict, or violence	1,895	366	1,528	43	131	417	395	80	608
A major change in family	3,572	1,356	2,215	131	190	441	630	292	633
Health reasons	713	226	487	21	48	118	87	210	259
To be closer to work or job	1,943	378	1,566	96	52	190	260	51	154
School or military	839	154	685	48	6	89	94	3	300
Wanted a better home or neighborhood	2,096	826	1,270	146	108	391	314	159	332
To be with or closer to family or friends	839	321	518	49	62	107	114	146	180
To establish own household	761	344	417	44	38	107	98	21	110
Other	3,159	990	2,169	191	147	584	485	335	762
Not reported	370	118	252	15	8	69	41	50	85
Previous Residence <sup>2</sup>									
Own place	14,044	4,381	9,663	651	721	2,190	2,216	1,207	2,799
Home of relatives/friends	4,417	1,198	3,219	142	265	755	762	247	1,237
Dormitories or barracks	228	46	182	14	2	30	27	10	73
Foster care	18	14	4	—	—	2	2	—	2
Treatment program, hospital, or nursing home	26	11	15	—	3	7	1	9	12
Jail or prison	15	6	9	—	—	—	1	1	9
Shelter or other homeless program	65	6	59	2	—	25	14	5	53
Place not meant for habitation <sup>3</sup>	21	—	21	—	—	3	2	2	6
Other	778	238	540	58	42	141	171	66	213
Not reported	341	102	239	14	13	69	46	59	78

**Source:** United States Census Bureau, 2013 American Housing Survey for the United States