BUILDING RACIAL AND ECONOMIC EQUITY THROUGH HOME OWNERSHIP

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OVERVIEW

California's commitment to racial justice and economic inclusion is meaningless without dramatic changes that make homeownership a possibility for marginalized racial and economic communities. Homeownership has been the most powerful vehicle for multigenerational wealth creation for the middle class.

In the middle of the 20th century, the tools for excluding communities of color from owning homes were overt and legal, creating a massive racial wealth gap. In California today, state and local zoning and the regulatory environment both contribute to exorbitantly expensive homes by constraining the supply of new housing and driving up the costs of those that are built.

Those policies and high housing costs have an outsized impact on Californians of color who tend not to have the intergenerational wealth increasingly needed to buy a home. In addition, the incredible expense of buying a home has led to a 50% drop, since 1980, in young Californians aged 18-34 who own a home.

These impacts are most pronounced in California's expensive coastal metropolitan areas and particularly so in Orange County, the Central Coast and Greater Los Angeles regions. Taking into account the median home cost and area median income (AMI), an astonishing zero percent of Californians of color - or in fact any Californians – making 60-150% of AMI can afford to purchase a home where they live in Orange County, the Central Coast and Greater Los Angeles regions.

The primary mechanism for providing housing that is affordable for people making near AMI has been the construction of homes required by deed restriction to be rented out at below market rates. Though that housing type will remain a part of the solution for specific circumstances, the massive $61.8 billion gap between what households making 60-150% of AMI can afford and the price of homes where they live cannot be solved through government subsidies alone.[1]

The main way for achieving this will be building more homes that are affordable by design. Currently, new homes built in California cost more than double the national average.[2] Complex regulations create uncertainty and delays that dramatically increase the price of new housing projects. Further, cash-strapped cities and municipalities have become more reliant on local impact fees, pushing prices up further.

This policy brief provides an overview of the dramatic racial wealth gap, the consequences of that gap for home ownership and current policies that need to be reformed to build more homes that are affordable by design. Without bold action to systematically lower the cost of new housing, California will fail to address the injustices that have systematically denied opportunities to Californians of color.

AFFORDABLE BY DESIGN

Affordable by design homes "cost less because they are small and efficiently designed."[3] Importantly these homes thoughtfully use design to maximize the quality of the space and do not require government subsidies in order for households near the regional Area Median Income (AMI) to afford them.[4,5] McKinsey estimates that "projects utilizing both nontraditional housing formats and prefab construction could reduce per-unit costs by some 50%—while minimizing the number of buildings that must go up and bringing more new housing online faster."[6]

1 The Legislative Analyst Office (LAO) issued a report in 2015 on California's housing costs that recommends recognizing the "targeted role of affordable housing programs." The $62 billion figure comes from an analysis of US Census Bureau microdata described later in this policy brief.

2 PolitiFact "Why it costs so much to build a home in the Golden State"

3 SPUR, "Affordable by Design: How to create middle income housing in San Francisco."

4 Sidewalk talk, City of the Future Podcast "Affordability by Design."

5 Low Rise, "Housing Ideas for Los Angeles."

6 McKinsey, "Affordable housing in Los Angeles: Delivering more—and doing it faster."

HOME OWNERSHIP AND THE RACIAL WEALTH GAP

Today's eye-watering prices push home ownership out of reach for more Californians who do not have access to generational family wealth or other financial support. Where homeownership opportunities have existed for communities of color, they are often disproportionately dependent on precarious and predatory financing structures that have undermined the ability of homeowners to sustain their ownership.[7,8,9]

Decades of discrimination have led to vastly disparate outcomes in household wealth. According to the Federal Reserve Bank of San Francisco, White households in Los Angeles have a median wealth of $355,000, more than 100 times the amount for Mexican-American households with $3,500 in median household wealth, and nearly as large a gap for Black households with $4,000 in median household wealth.[10]

The lack of generational wealth and dramatic rise of housing costs have made the dream of home ownership increasingly unattainable for Californians of color. In 1980, a typical California home cost about three times what a typical household made. Today a typical home costs about nine times what a typical household makes.[11] That significant increase makes it that much more difficult for homebuyers without access to wealth.

The following recommendations are in development by the California Economic Summit Work Group led by:

- **Darius Assemi,** President, Granville Homes
- **Dan Dunmoyer,** President and CEO, California Building Industry Association
- **John Gamboa,** Vice-Chair, The Two Hundred
- **Lori Gay,** CEO, Neighborhood Housing Services of Los Angeles County
- **Jennifer Hernandez,** Partner, Holland and Knight
- **Jennifer LeSar,** President and Founding CEO, LeSar Development Consultants
- **Tia Boatman Patterson,** Executive Director, California Housing Finance Agency (former)

Preliminary Recommendations of the Expanding Home Ownership Work Group

1. Maximize the ability of the private marketplace to meet California's affordable homeownership goals as the primary vehicle for achieving racial and economic equity.

Our strategy should maximize the ability of the private marketplace to help regions in California meet ambitious Regional Housing Needs Allocation (RHNA) goals and produce the housing supply and types that we need in California at price points affordable to 60-150% area AMI households comprised of communities of color.

2. Provide targeted solutions where the market will continue to fail without augmentation.

Where the marketplace falls short of meeting these goals, we should identify and prioritize scalable solutions to drive homeownership through the lens of equity and parity among racial and ethnic groups, gender, and geographical regions.

3. Advocate for scalable capacity building where needed to meet California's affordable homeownership goals.

We should recognize where capacity development may be essential to produce the housing that is needed and should then identify and prioritize scalable solutions to meet our goals. Those include support for local planning departments, expanding the pipeline of skilled tradespeople, increasing education for first time homebuyers, and augmenting programs to increase the strength of Black, Indigenous, People of Color and women led developers.

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7 Mapping Inequality: Redlining in America.

8 Segregated by Design.

9 See for example this reality during the housing bubble: "For instance, Blacks who obtained their loan through a mortgage broker were 10% more likely to receive a subprime ARM than those who went through the retail side of the bank, and 13.5% less likely to receive a prime ARM if they obtained their loan through a federally regulated institution within its CRA assessment area." (San Francisco Federal Reserve)

10 "The Color of Wealth in Los Angeles," San Francisco Federal Reserve.

11 US Census Bureau.

REALITY OF BUYING A HOME IN CALIFORNIA

First time home ownership in California increasingly requires family support. Approximately one in four California Federal Housing Administration loans, a type of federal assistance for lower down payment loans, included down payment money from the buyer's family in 2011, a number that has since increased to one in three.[12] In San Jose, 48% of houses had sales deeds that listed multiple non-married buyers, which often signals that parents are co-buying with their children. In San Francisco, that figure is 38%. Additionally, a growing number of all-cash buyers are wealthy parents supporting their children.[13]

That type of parental financial support is not available to many Californians of color. Home ownership for Black Californians has declined over 20% since 1980. More broadly, home ownership for young Californians aged 18-35 has fallen by almost half during the past four decades.[14] This figure reflects the growing population of young Californians who cannot, on their own, secure a mortgage.

Additionally, the share of young adult Californians living at home with their parents has increased to nearly four in 10, outpacing the nation and almost double the rate in 1980.[15] Young Californians living at home are also 15% more likely to be Asian or Black than White and 30% more likely to be Latino than White.[16]

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12 CalMatters, "Where do people get money to buy California homes these days? Often, from mom and dad"

13 KPCC, "Who are the cash buyers in SoCal real estate?"

14 US Census Bureau Public Use Microdata (PUMs).

15 CalMatters, "Amid housing crisis, why 2 out of 5 young Californians live at home." Updated in 2019.

16 IBID

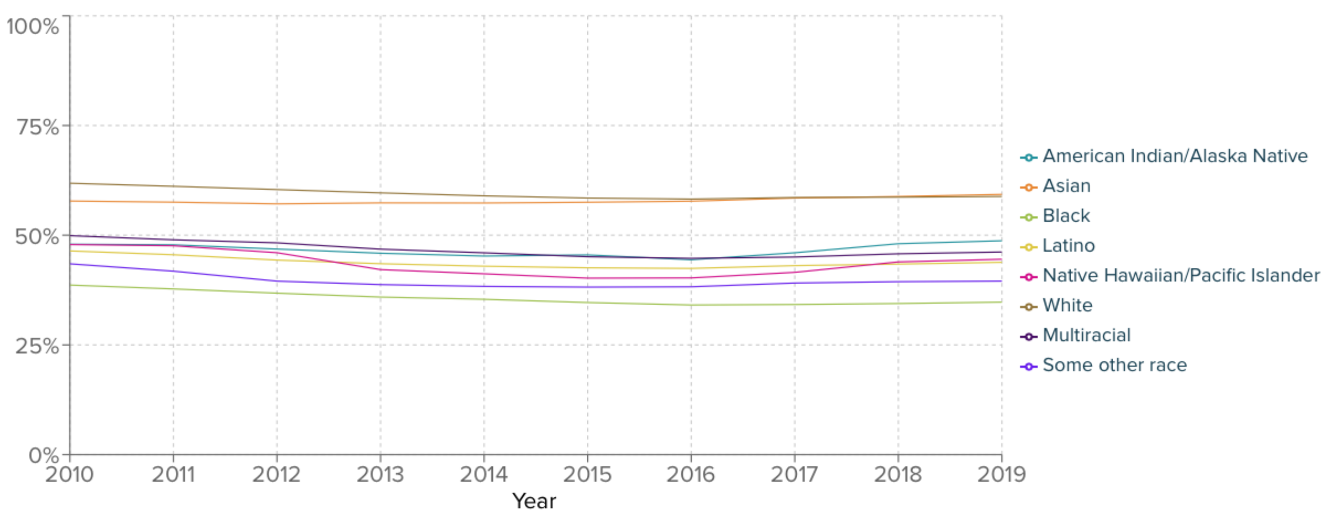
Over the last decade California home ownership rates have stagnated.[17] According to the Federal Reserve Bank of St. Louis, California ranks 49th of the 50 states in home ownership. This represents a tremendous barrier for Californians looking to build wealth. More broadly, high housing prices make it much more difficult for California families to meet basic needs such as food, healthcare and transportation.

CALIFORNIA DREAM INDEX

The California Dream Index tracks progress toward a more equitable California where all can prosper. Measuring 10 trackable indicators for economic mobility, security and inclusion through one powerful platform, data can be analyzed by race and ethnicity, region, and county, providing the ability to do "apples to apples" regional comparisons across the state. The tool, launched in December 2020 by California Forward, includes indicators on home ownership and income above cost of living.

The Index indicates that even after a decade of economic growth, home ownership rates have declined 4.5% since 2010. During that same period home ownership rates declined over 11% for Black Californians and 6% for Latino Californians. Today 35% of Black households, 44% of Latino households, 59% of Asian households and 59% of White households own their home in California.

THE PERCENT OF HOUSEHOLDS WHO OWN THEIR PRIMARY RESIDENCE



CALIFORNIA DREAM INDEX

17 California Dream Index.

IMPACT OF HIGH HOME PRICES

Mostly as a result of high housing costs, the United Way of California recently showed that 38% of Californians, or over 3.8 million families, could not reliably pay monthly expenses — even after a decade of economic growth.[18] Sixty percent of families with young children struggle to pay the most basic monthly living expenses. Those struggling families are predominantly Latino and Black. Moreover, those figures were before COVID-19 exacerbated economic inequality.

Additionally, Californians are commuting further and further in order to live in affordable communities. Over the last decade, commute times have increased nearly 11%. Black Californians in particular have 7.5% longer commutes than the state average.[19] In addition, growing numbers of low-income Californians have left the state.[20]

These hard realities are the direct consequence of skyrocketing housing prices that make home ownership unattainable where people live and work. The chart below shows the percent of Californians of color making 60-150% of regional Area Median Income (AMI) that are able to afford the monthly payment for a home where they live. An astonishing zero percent of Californians of color making 60-150% of their groups Regional AMI can afford a typical home where they live in Greater Los Angeles, Orange County and the Central Coast.[21]

PERCENT OF CALIFORNIANS OF COLOR MAKING 60-150% REGIONAL AMI ABLE TO AFFORD A HOME WHERE THEY LIVE

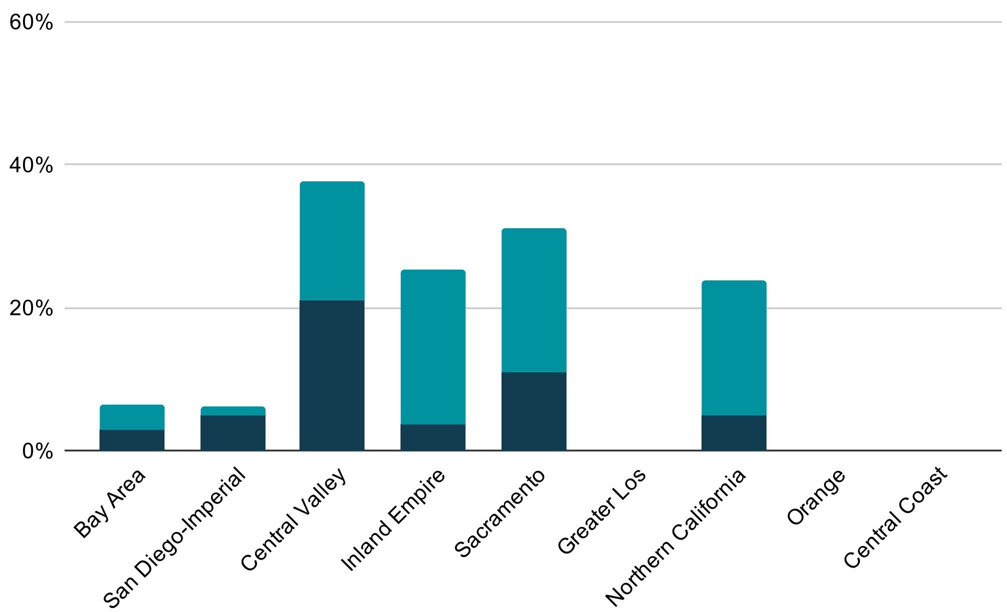


Figure 1: Californians of Color include Latino, Black, Native American, and other and biracial Californians. The monthly payment is calculated assuming an interest rate of 3%, 30-year fixed mortgage with 0.22% of the home value for home insurance and 1.15% of the home value for property taxes.

- Additional percent of people able to afford a home w/ 30% of income
- Percent of people in 60-150% of AMI able to afford a home w/ 25% of income

18 United Way Real Cost Measure.

19 California Dream Index.

20 California Legislative Analyst's Office, "California Losing Residents via Domestic Migration."

21 This analysis utilizes the standard threshold of 30% of a household's income to determine an affordable housing payment. The precise threshold for a given household is very dependent on their specific financial circumstances. The California Housing Financing Agency provides loans to many middle- and low-income Californians in the 40-45% range and provides additional down payment assistance to qualified borrowers. Those programs are important steps forward to expanding home ownership though the long-standing impacts of systemic racism and magnitude of the home ownership gap calls for systemic solutions.

CALIFORNIANS MAKING 60-150% REGIONAL AMI ABLE TO AFFORD A HOME WHERE THEY LIVE

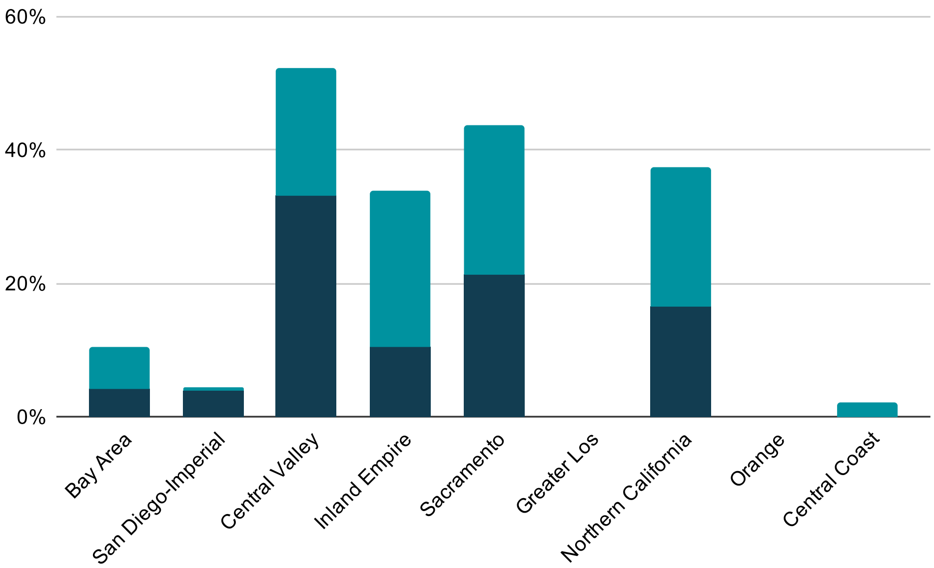


Figure 2: This chart is the same as Figure 1 except it includes all Californians of all racial groups.

Housing affordability in California varies by region. The ratio of median home price to median income is approximately 20% above the national average in the Sacramento region and Inland Empire and 10% higher in the Central Valley. By contrast, coastal California including the Bay Area, Greater Los Angeles, Central Coast and Orange County range from 80-100% higher.

	Typical home price that California Latino, Black, and Native American households can afford	Typical home price in the county where a household lives	Ratio of typical price to price people can afford
Bay Area	$519,438	$1,058,620	2.04
Central Coast	$371,709	$703,885	1.89
Central Valley	$238,831	$270,146	1.13
Greater Los Angeles	$317,440	$639,687	2.02
Inland Empire	$304,742	$371,534	1.22
Northern California	$241,254	$289,814	1.20
Orange	$387,891	$768,414	1.98
Sacramento	$336,016	$410,165	1.22
San Diego-Imperial	$335,846	$596,953	1.78

There is a $61.8 billion gap between the home price that California households making 60-150% of Area Median Income (AMI) can afford and the typical home price where these Californians live.[22] Of that gap, Latino, Black and Native American Californians are disproportionately affected with a $35.5 billion gap or 58% of the total in spite of being 45% of the population.

$61.8 BILLION GAP

Between the home price Californians making 60-150% of AMI can afford and the cost of a typical home where they live.

The magnitude of that gap highlights the challenges of achieving affordability primarily through government subsidies and the importance of building homes affordably by design. This is critical for expanding home ownership as economic research shows that building affordable by design "contribute[s] directly to a lower housing cost burden for the families that reside within them."[23]

22 Authors calculations from US Census Microdata and Zillow. The housing price a household can afford is calculated using the same methodology as the regional chart above and assumes an interest rate of 3%, 30-year fixed mortgage with 0.22% of the home value for home insurance and 1.15% of the home value for property taxes. The $61.8 billion figure is the sum of the difference between those affordable home prices for each household and the actual median home price in the county that each household lives in.

23 Bay Area Council Economic Institute, "How Policies Change the Number of San Francisco Households Burdened by Housing Costs."

BARRIERS TO BUILDING AFFORDABLY BY DESIGN

California's high home prices are not an accident nor solely a consequence of California's unique characteristics.[24] While portions of the state, primarily coastal California, have much higher land prices and labor costs, policies that add additional fees and delays make new housing construction prohibitively expensive, particularly for Californians of color.

In a highly regarded report titled "Making it Pencil," the Terner Center at UC Berkeley explained the math behind California housing development.[25] This analysis showed the various costs that go into the development of new housing and how various requirements impact the ability of developers to secure financing and deliver projects.

Even under conditions that omitted key cost drivers like litigation and the threat of litigation associated with the California Environmental Quality Act (CEQA), the rental price for a two-bedroom apartment in the East Bay requires 164% of the Bay Area's very high median income to be affordable for a household. Home prices, even at the lower end of the market, are similarly out of reach for households making at or near the regions median income as shown in Figure 1. Layering in additional common requirements like extra parking, higher development fees, and inclusionary housing requirements make the projects financially infeasible even with unaffordable rents.

24 The cost of California's housing regulatory regime is described in detail for the San Diego market by the Fermanian Institute at PLNU's report, "Opening San Diego's Door to Lower Housing Costs."

25 The report examines the cost drivers for new apartment rentals though the factors are illustrative for home ownership as well. The Terner report focused on a prototypical multi-use multifamily apartment complex with 120 units under assumptions that ignored factors like litigation under the California Environmental Quality Act, demolition or environmental remediation, or prevailing wage rules. Those initial conditions were then layered with common policies and requirements to show how those additional policies increase housing prices.

Notably, none of the scenarios that Terner analyzed included litigation or the threat of litigation associated with CEQA, which can add substantial professional services and financing costs for project delays. In 2018, 60% of all CEQA petitions targeting private sector projects were filed against housing.[26] Those CEQA induced delays increase a project cost exponentially due to compound interest from the cost of capital.

Further, Terner assumed $40,000 per unit in developer fees. These fees vary dramatically as detailed in the Terner study titled "It All Adds Up: The Cost of Housing Development Fees in Seven California Cities," ranging upwards of $60,000 per multifamily unit and $140,000 per single family home in Irvine and Fremont.[27] A similar methodology was used for single-family residential and apartment complexes in Southern California by John Husing of Economics and Politics, Inc., who found similar issues with housing affordability in Southern California.[28] Neither Los Angeles nor inland Orange County could build apartment complexes affordably by design. Only in the Inland Empire was that possible, yet even there, higher fee costs and lower revenue from inclusionary housing requirements would make the resulting units unaffordable to the median income household.

A similar approach was utilized by Husing for single-family residential homes and reached similar results. The analysis showed that only the Inland Empire had the conditions to build single-family homes that met the affordability threshold of 30% of household income for conventional 20% down financing. Federal Housing Administration (FHA) loans with a much lower down payment resulted in an unaffordable monthly cost. The addition of any fees or inclusionary housing requirements without offsets resulted in projects unaffordable to both types of buyers.

The studies by Husing and the Terner Center provide an overview of the economics of building housing and the general policy barriers to building affordably by design. Several caveats must be made, however. For example, high-rise condominium and apartment complexes over approximately seven stories require a "shift from wood frame building materials to concrete and steel, which raises the overall cost of a project considerably."[29] The state housing conversation would benefit from additional research into the economics of developing "missing middle" housing such as townhomes, duplexes, triplexes, quads, modular construction and other types of housing that are affordable by design.

At the state level, over the course of the last decade California has developed additional green building standards that add $22,000 - $30,000 to all types of new homes.[30] Though providing a social benefit, this pushes many projects well beyond median income affordability as shown in the Terner and Husing report analyses.

In addition, in December 2018 California adopted new regulations for implementing CEQA that include a new environmental impact called Vehicles Miles Traveled ("VMT"). This requires projects to offset the impact of driving, even after adoption of zero emission vehicles, in favor of walking, biking and public transit. According to the California Building Industry Association (CBIA), providing transit passes to meet the offset requirements increases the price of a home over $70,000, making new homes even more expensive for Californians of color.

Weighing the policy benefits of those green policies against the costs is beyond the scope of this policy brief. It is notable, however, that these requirements apply only to new housing construction and predominantly affect new homebuyers, a group that tends to be younger and more diverse than California as a whole.

Cumulatively these requirements make new home construction expensive, often prohibitively so, and result in conditions that make home ownership for Californians of color virtually impossible in coastal California and a severe stretch across the state.

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26 "California Getting in its Own Way" authored by Jennifer Hernandez and edited by Joel Kotkin

27 Terner Center, "It All Adds Up."

28 "Housing Market Feasibility & Affordability Study Southern California," prepared for the Building Industries Legal Defense Foundation.

29 Terner Center, "Making it Pencil: The Math Behind Housing Development."

30 California Building Industry Association, "Cost Impact of Recently Adopted and Proposed Building Standards" from 2010-2017.

CONCLUSION

Addressing California's high housing costs is critical to building opportunity for all Californians, particularly Californians of color who have been systematically excluded from the benefits of growing wealth from rising housing prices. California will not make progress on achieving racial equity without reforming policies that make home ownership prohibitively expensive for Californians of color.

> **The $61.8 billion gap between what communities of color can afford and the typical home price where they live in California cannot be solved through government subsidies alone. The best strategy to address California's housing crisis and ensure home ownership is a realistic goal for Californians of color is to build new housing that is affordable by design.**

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