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An Assessment of the American Housing and Economic Mobility Act of 2021

INTRODUCTION

The nation is struggling with an affordable housing crisis. There is not enough housing for sale or rent in communities across the country. This means families must pay more for their housing, renters have less to get by on at the end of the month, homeownership is out of reach for too many, and those of modest means are forced to live farther from decent jobs. This has significant economic and social repercussions. The American Housing and Economic Mobility Act of 2021 would help address this mounting housing crisis.

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BY MARK ZANDI

The nation is struggling with an affordable housing crisis.[1] There is not enough housing for sale or rent in communities across the country. This means families must pay more for their housing, renters have less to get by on at the end of the month, homeownership is out of reach for too many, and those of modest means are forced to live farther from decent jobs. This has significant economic and social repercussions. The American Housing and Economic Mobility Act of 2021 would help address this mounting housing crisis.[2]

Affordable housing crisis

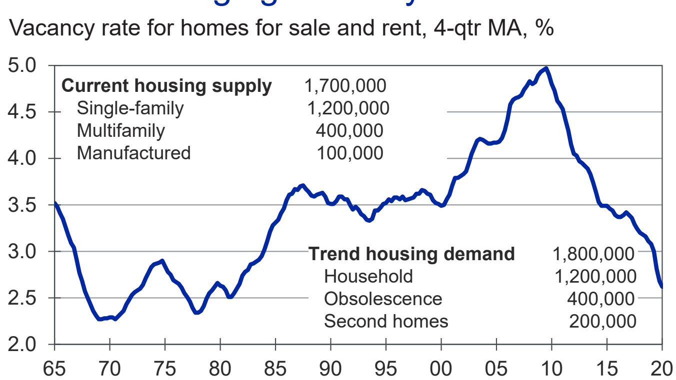
Homebuilding collapsed during the housing crash over a decade ago and has been slow to recover. Construction of high-end homes and apartments recovered first, and there is now an oversupply in some urban areas across the country. However, the construction of affordable housing—homes reasonably priced for lower-income households to rent or own—has only recently begun to increase and continues to lag demand.

The worsening affordable housing shortage is clear in the low number of vacant housing units, which continues to decline. The percent of the housing stock for rent and sale that is unoccupied has fallen sharply since the housing crash and is now as low as it has been in more than 30 years (see Chart 1). The shortfall in affordable housing is close to an estimated 1.8 million homes, equal to more than a year of new construction at its current pace.

And this housing shortage continues to get worse. The current annual supply of new housing units is still running an estimated 100,000 below the trend for new-housing demand. Total supply equals new single- and multifamily units and manufactured homes, and trend housing demand equals household formations, new homes needed to replace those that become obsolete, and second and vacation homes. Trend demand abstracts from the near-term temporary ups and downs in demand.

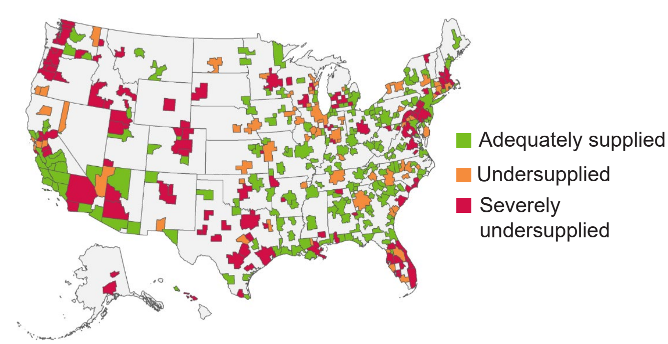
Even these figures understate the severity of the problem. The lion's share of the undersupply is concentrated in the lower end of the market, particularly in areas that offer significant economic opportunity, driving up house prices and rents for low- and moderate-income families precisely where they want to live (see Chart 2).[3] Prices for homes sold in the bottom quartile are up nearly 8% per annum over the past decade, almost double that for homes in the top quartile. And rents

Chart 1: Plunging Vacancy Rate



Sources: Census Bureau, Moody's Analytics

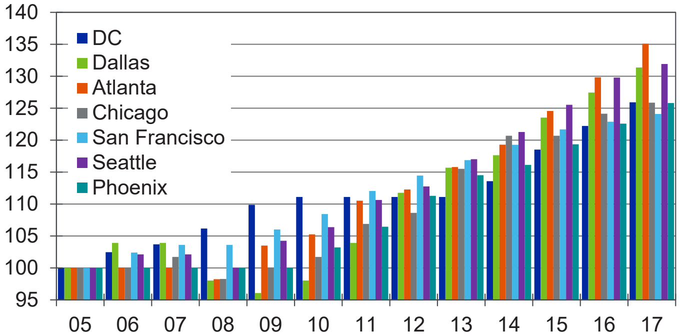
Chart 2: Shortages Across the Country



Sources: Census Bureau, Moody's Analytics

Chart 3: Increased Congestion

Hrs of traffic delay per person, 2005=100



Sources: Texas A&M, Moody's Analytics

for those families who rent because they cannot afford to own, rather than by choice, have increased nearly 4% per annum over the past decade—a trend that has continued even during the pandemic.

The rising rents leave more and more renters with little to live on. Today, one in four renters pays over half of their monthly income toward rent, leaving barely enough to cover food, clothing and healthcare, much less save for emergencies or build wealth. The typical renter saves less than $500 a year, not enough to cover run-of-the-mill financial emergencies let alone save for a down payment on a home. And the rise in house prices is putting the economic opportunity of homeownership out of reach for more and more families, particularly those of color. Today the homeownership rate for Hispanics is 48% and for Blacks it is 42%, a level not seen in decades.[4]

The housing shortfall is not just depressing savings and increasing the wealth gap. It is also forcing those at the bottom of the economic ladder to live farther away from those at the top and, more importantly, farther from economic opportunity. The most desirable cities are becoming affordable only to the wealthy, while many of those of more modest means are forced into longer commutes, creating more traffic, more environmental strain, and greater social division (see Chart 3).

Homebuilding constraints

Homebuilders have steadily increased production of new housing since the housing crash. During the worst of the downturn a decade ago, builders put up only 600,000 homes per year. New construction today is approaching 1.7 million units. Yet much of the increase in homebuilding has been at the high end of the housing market. Demand by higher-income households recovered more quickly from the recession, and the higher house prices and rents builders could charge these households have been a strong incentive to build more.

Construction of affordable housing—homes that low- and moderate-income households can afford to rent or buy—has been much slower to bounce back. The story is one of demand and profit margins. Low- and moderate-income households were much slower to recover from the recession, only hitting their economic stride again in the year or two before the pandemic. And the profit margins that builders could get from building affordable housing have been too low to incent the investment, with pricing too low to adequately clear the high fixed costs of building.

The economics of building affordable housing have improved more recently, with skyrocketing house prices and rents finally creating a wide enough profit margin to justify more investment. But the fact that the economics of building affordable housing are still precarious and appear to require pricing that is not affordable for many homebuyers and renters, especially as mortgage rates normalize on the other side of the pandemic, indicates the problem remains acute.[5]

Meanwhile, the constraints on building affordable housing units, including building materials and labor, lending, and land, remain significant. These are key inputs into building a home, and they have all been in short supply since the financial crisis, driving up their cost and reducing builders' profit margins and thus their incentive to put up more homes, particularly lower-priced housing with lower margins.[6]

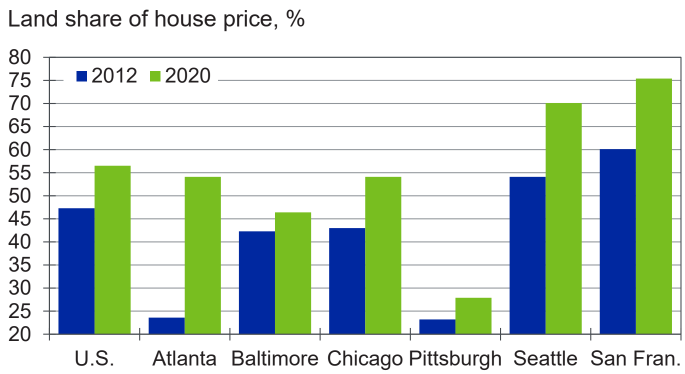
While prices of many building materials have risen in recent years, the rise in softwood lumber prices has been especially dramatic, up close to 10% per annum since the housing bust and nearly double over the past year alone.[7] The higher material costs reflect a range of factors, most recent being the disruption of global supply chains during the pandemic and the Trump administration's imposition of higher tariffs and greater trade restrictions on most major U.S. trading partners.

Homebuilders have also struggled in recent years to develop and maintain a consistent labor force, reflecting the difficulty that many of the trades face in attracting high school graduates into careers requiring specialized skills. Prior to the financial crisis, this labor gap was largely being filled by immigrants. But, just as housing demand began to warrant ramping up housing supply again, the Trump administration all but shut down this source of labor through restrictive immigration policies. Labor cost pressures have eased a bit during the pandemic, but this appears temporary and will almost surely worsen again if there is a large federally financed infrastructure effort.[8]

As the cost of materials and labor has gone up, builders' access to financing has gone down. Bank acquisition development and construction lending is an especially important source of financing for smaller builders who often do not have ready access to other forms of financing.[9] Yet banks have been pulling back on these loans since the financial crisis and show little signs of expanding them again. The retreat has been strongest for smaller banks that cater to smaller builders. This constrains supply at the lower end of the housing market, where smaller builders often focus.

The most significant impediment to building more affordable housing is the availability and cost of land. There simply is not enough buildable land to meet the demand in many areas, and the costs associated with securing and developing the land that is available too often push builders' total costs above what they could get from the sale of an affordable property. The cost of land has soared to an estimated 55% of the total price of the median-priced home nationwide, and upwards of 70% in high-opportunity areas such as Seattle and San Francisco (see Chart 4).[10]

Chart 4: Land Costs Soar



Sources: CoreLogic, Engineering News Record, Moody's Analytics

American Housing and Economic Mobility Act

The American Housing and Economic Mobility Act provides just over $500 billion in federal support over the next decade to alleviate the shortage of affordable housing units (see Table 1). This is done through funds to incent localities to ease regulations and other building restrictions and provide down payment assistance to lower-income first-time homebuyers living in low-income communities. Most significantly, the funds are to be used to scale up the Housing Trust Fund and Capital Magnet Fund. The plan is paid for by scaling back estate tax exemptions and other reforms.[11]

The HTF and CMF were established by the 2008 Housing and Economic Recovery Act, but funding began only a few years ago. Current combined funding is several hundred million dollars a year based on a fee charged on loans purchased by Fannie Mae and Freddie Mac. The HTF provides funds to state housing authorities for the development of affordable rental units. Housing authorities have flexibility in allocating these funds, since each has different objectives and goals based on the needs of the local population. The CMF provides funds to Community Development Financial Institutions and other nonprofit developers for increasing the supply of affordable housing. CDFIs are mission-driven financial institutions that provide financing for development in underserved communities. The HTF and CMF have the flexibility necessary to significantly increase the supply of affordable housing in real estate markets encumbered by a range of complex and costly problems.

The American Housing and Economic Mobility Act is designed to be deficit neutral on a dynamic basis over the 10-year budget horizon. The costs of these affordable housing initiatives are paid for by reforms to the estate tax, most importantly by rolling back estate tax exemptions to their 2009 levels.

Housing and economic impact

The Moody's Analytics model of the U.S. economy is simulated to determine the impact of the expansion of the HTF and CMF in the American Housing and Economic Mobility Act on housing and the economy.

The simulation is based on several assumptions, including that the legislation becomes law later this year and takes effect in 2022. It also assumes there are no other fiscal policy changes other than what are in current law and that monetary policy is endogenously determined—the model is used to determine how the Federal Reserve manages short-term interest rates and its quantitative easing program.

Another important assumption is that it will cost close to $200,000 to produce a typical affordable housing unit in 2022. This is consistent with the cost to produce a unit in a Low-Income Housing Tax Credit project. We expect that cost to increase more than 3% per annum in the next several years, given the strengthening economy and ongoing global supply chain problems, and to moderate closer to 2% growth by the second half of the 2020s, consistent with overall price inflation.

Given the magnitude of the increase in funding for the HTF and CMF, Moody's Analytics assumes it will take several years to get these programs up to full speed. Each will need some time to expand its infrastructure for evaluating uses of the increased funds and disbursing them effectively. The American Housing and Economic Mobility Act does not change current law with regard to how

Table 1: Economic Impact of American Housing and Economic Mobility Act of 2021

	Annual spending, $ bil			Additional affordable housing units			
	Housing Trust Fund	Capital Magnet	Total	Housing Trust Fund	Capital Magnet	Total	Additional jobs
2022	34.5	0.4	42.2	171,969	13,957	222,351	300,301
2023	40.0	0.9	41.0	193,953	30,548	224,986	303,860
2024	43.0	1.7	44.8	203,415	56,294	260,181	351,394
2025	44.5	3.0	47.6	205,778	97,108	303,348	409,695
2026	46.0	3.1	49.2	208,135	98,185	306,773	414,319
2027	47.0	3.1	50.2	208,286	96,166	304,895	411,783
2028	47.5	3.2	50.8	206,172	97,226	303,832	410,348
2029	47.5	3.2	50.8	202,129	95,320	297,875	402,302
2030	47.5	3.2	50.8	198,166	93,451	292,034	394,414
2031	47.5	3.2	50.8	194,280	91,618	286,308	386,680
2022-2031	445.0	25.0	478.2	1,992,282	769,873	2,802,582	

Note: Total includes the HTF, CMF, and various other smaller programs in the legislation.

Source: Moody's Analytics

the HTF and CMF operate. Under current law, at least 70% of CMF funds must be used to support affordable housing projects, and no more than 10% of an affordable housing project's costs can come from the CMF. These and other rules under current law slow the disbursement of funds and are key to why it takes several years to ramp up the production of affordable housing.

Under the legislation, our model shows that affordable housing construction increases by close to 225,000 units in 2022, increasing to over 300,000 units annually by mid-decade. Over the 10-year budget horizon through 2031, affordable housing production increases by 280,000 units per annum on average. This would more than fill the current shortfall in annual affordable housing construction and would at worst quell the affordable housing crisis by the end of the decade. The crisis should come to an end even sooner if market forces continue to support more construction, which is likely if the American Housing and Economic Mobility Act eases regulatory restrictions on affordable homebuilding as anticipated.

Since the legislation significantly increases housing supply, it will have the added benefit of improving housing affordability, particularly for affordable rental homes. Without the legislation, rents are expected to increase by approximately 4% per annum. With the legislation, rent growth will be near 3% per annum. A decade from now, affordable rents will be approximately 10% lower than they are today, or about $100 per month in today's dollars.

More housing construction will increase the economy's growth rate and the number of jobs as activity increases. In 2022, the increased housing construction will lift employment by 250,000 jobs and by as much as 400,000 jobs at the peak of the impact in the mid-2020s.

There is very little impact on the economy and jobs from the scaling back of the estate tax exemptions and other reforms. The wealthy households that will pay more in estate taxes have substantial financial resources and will not significantly change their spending and saving behavior. Moreover, since the increased tax revenues pay for the expansion of the HTF and CMF and other programs, it ensures that the American Housing and Economic Mobility Act is deficit neutral, with no resulting impact on interest rates.

This simulation likely understates the economic benefit of the legislation, because it does not consider that the measure will facilitate the ability of low-income households to move closer to their employment or potential jobs. The housing shortage and erosion in affordability are constraining the ability of low-income households to take the record number of open job positions that are currently available in places where housing is simply too expensive. Affordability is also forcing low-income workers to live farther away from their work, requiring long and costly commutes and reducing productivity.

Conclusions

More than a decade after the housing crash and financial crisis, the nation is still suffering a housing crisis. A decade ago, the problem was egregious mortgage lending and overbuilding. Today, it is a mounting lack of affordable housing. Low-income and minority households are struggling to make their rent and mortgage payments, suffering through increasingly long commutes, and unable to take better jobs because they cannot afford housing near the available work. The American Housing and Economic Mobility Act would help to address these problems. It is fiscally responsible legislation that empowers programs that are already in place and shown to be effective in meeting the challenges of providing affordable housing to low-income households and underserved communities.

Endnotes

1 This white paper relies heavily on "*Overcoming the Nation's Daunting Housing Supply Shortage*," Parrott and Zandi, Urban Institute and Moody's Analytics white paper, March 2021.

2 Massachusetts Senator Elizabeth Warren initially introduced the American Housing and Economic Mobility Act in September 2018. Moody's Analytics evaluated the economic impact of this legislation in "Addressing the Affordable Housing Crisis," Mark Zandi, Moody's Analytics white paper, September 2018. The currently proposed legislation, the American Housing and Economic Mobility Act of 2021, makes only small changes to the 2018 legislation. Our economic analysis of the 2021 legislation shows somewhat lower new housing production than in the analysis we did of the 2018 legislation due to the significant increase in housing construction costs over the past several years. However, the estimated employment impacts of the 2021 legislation are meaningfully less than those estimated in 2018 because of different assumptions concerning the mix of new single- and multifamily homes that will be constructed due to the legislation. We now expect the construction of substantially more multifamily units, which results in just over one full-time equivalent job, and fewer single-family homes, which supports closer to three full-time equivalents. The change in our estimated employment impacts is not due to a change in the legislation, but a change in the assumptions underpinning our analysis.

3 See "*Housing Constraints and Spatial Misallocation*," Hsieh and Moretti, American Economic Journal: Macroeconomics, 2019.

4 These homeownership rates are for 2019 from the Census Bureau's Housing Vacancy Survey. The HVS for 2020 has significant measurement problems due to the pandemic.

5 In an economy operating at full employment and with inflation at the Federal Reserve's 2% target, fixed mortgage rates will be near 5.5%.

6 The *National Association of Home Builders' 2019 Construction Cost Survey* provides a good breakdown of the costs involved in building a typical single-family home.

7 This is for the producer price index for softwood lumber from the Bureau of Labor Statistics. Random Lengths data indicate that softwood lumber prices are up even more, from $350 per thousand board feet in April 2020 to $1,040 in March 2021. The National Association of Home Builders estimates this has added $24,000 to the price of a typical home.

8 This is based on the employment cost index for construction workers from the Bureau of Labor Statistics.

9 This includes one- to four-family residential construction loans and land development loans from the FDIC.

10 We estimate land values and the land share of house price across metropolitan areas based on data from the FHFA, CoreLogic, and the Engineering News Record. The FHFA land value methodology and estimates are available from "*The Price of Residential Land for Counties, ZIP codes, and Census Tracts in the United States*," Larson, Shui, Davis and Oliner, FHFA working paper, November 2020.

11 To be more precise, the American Housing and Economic Mobility Act of 2021 is deficit neutral over the 10-year budget horizon on a dynamic basis, which accounts for the benefit of the plan on the economy and thus on the government's finances.

About the Author

Mark Zandi is chief economist of Moody's Analytics, where he directs economic research. Moody's Analytics, a subsidiary of Moody's Corp., is a leading provider of economic research, data and analytical tools. Dr. Zandi is a cofounder of Economy.com, which Moody's purchased in 2005.

Dr. Zandi is on the board of directors of MGIC, the nation's largest private mortgage insurance company, and is the lead director of Reinvestment Fund, one of the nation's largest community development financial institutions, which makes investments in underserved communities.

He is a trusted adviser to policymakers and an influential source of economic analysis for businesses, journalists and the public. Dr. Zandi frequently testifies before Congress and conducts regular briefings on the economy for corporate boards, trade associations, and policymakers at all levels. He is often quoted in national and global publications and interviewed by major news media outlets, and is a frequent guest on CNBC, NPR, Meet the Press, CNN, and various other national networks and news programs.

Dr. Zandi is the author of *Paying the Price: Ending the Great Recession and Beginning a New American Century*, which provides an assessment of the monetary and fiscal policy response to the Great Recession. His other book, *Financial Shock: A 360º Look at the Subprime Mortgage Implosion, and How to Avoid the Next Financial Crisis*, is described by the New York Times as the "clearest guide" to the financial crisis.

Dr. Zandi earned his BS from the Wharton School at the University of Pennsylvania and his PhD at the University of Pennsylvania.

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