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Crowded out of the housing market

Declining affordability and availability are squeezing New England's very low-income households

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Though many New Englanders find it difficult to buy and maintain a home or pay monthly rent, the problem is particularly acute for the region's very low-income households. While many reports about housing affordability focus on the growing affordability challenges faced by middle-income households, they often overlook a crucial problem in the region: very low-income households—those in the bottom fifth of the income distribution—are squeezed by declining affordability *and* limited availability.

The annual incomes of many of the region's poorest households have not increased in real terms for some time. And over the past decade, their modest budgets have been squeezed even further as house prices have appreciated rapidly, especially at the lower end of the housing distribution. As a result, the vast majority of very low-income households spend more than 30 percent of their income on housing costs, an amount most industry experts consider unaffordable. Additionally, the rapid growth in house prices seems to have pushed higher-income households to seek cheaper housing options, crowding very low-income families out of places that they could otherwise afford. Crowding out is especially worrisome for the region's very low-income households for two reasons: the supply of housing affordable to this group was woefully inadequate to begin with and these households often have nowhere else to go.

> While real incomes have declined, house prices have soared

The squeeze

While housing costs have always taken a bigger bite out the incomes of low-income households than of high-income households, two diverging trends have widened the gap in recent years. First, over the past five years, the real incomes of very low-income households in many New England states have fallen while those of their middle-income counterparts have risen.[1]

In 2005, New England's very low-income households—those occupying the bottom fifth of the income distribution—earned a median annual income of $12,475, 6.7 percent less in real terms than they earned in 2000.[2] By comparison, New England's middle-income households—those occupying the middle fifth of the income distribution—saw real median income grow by 2.1 percent over this period.

The second trend is less obvious. Even as the incomes of very low-income households have been declining, the prices of the homes they would most likely buy have been appreciating even more rapidly than the median-priced house. Detailed house price data for Connecticut, for example, show that prices for the least expensive houses—those at the tenth percentile of the housing distribution—increased by 71.1 percent between 1999 and 2005, while the median-priced house appreciated by 47.9 percent over the same period. Another study shows a similar divergence between 2001 and 2003 in the Greater Boston area.[3]

As a result, declining housing affordability has removed ownership further from the reach of low-income households than other groups. Again using Connecticut as an example, very low-income households earned about half the income needed to purchase a house at the tenth percentile of the housing distribution in 1999 but less than one-third of the income needed in 2005. Even though affordability for middle-income households also declined over this period, middle-income households still earned about two-thirds of the income needed to purchase the median-priced house in 2005. While middle-income households might be able to stretch to afford the median-priced home or could choose to live in less expensive homes, very low-income households realistically do not have these options.

Why not rent? It may not be the American Dream, but not all very low-income households buy a house; in fact, more than half do not. In 2005, roughly 56 percent of New England's very low-income households were renters. Not surprisingly, very low-income renters also fared worse in terms of affordability relative to their middle-income counterparts. About 75 percent of very low-income renters were considered cost-burdened in 2005, meaning they spent more than 30 percent of their income on rent, and nearly half were severely cost-burdened, spending more than 50 percent of their income on rent. By contrast, less than one in seven middle-income renters was cost-burdened, and less than 1 percent was severely cost-burdened.

Crowding out

Even if New England's very low-income households are able to stretch to afford the least expensive apartments, the supply of available units in that price range may not be adequate to meet demand. If so, the region still has an affordability problem. Our analysis suggests that rapid house price appreciation over the past decade encouraged higher-income households to seek cheaper housing options, a situation that is likely to occur when supply is constrained. Middle-income households, unable to afford the median-priced housing in their area, seem to have moved down the housing distribution to occupy cheaper single-family homes or rental units.

To examine whether there is a sufficient supply of rental units affordable to very low-income households, we looked at two measures. First, we compared the number of units that are affordable to households in a given income range to the actual number of households in that income range. Second, we compared the number of affordable units to the number of households in a given income range, excluding those units that are occupied by higher-income households. The second measure indicates whether the potential supply of affordable units is actually available for a given income group.

Using these two measures, we found that the supply of affordable housing for both middle-income and very low-income households is inadequate, in part because of crowding out by higher-income households.

Table 1: Declining real incomes and rising costs have made rental housing less affordable for very low-income households

	Median annual household income			Share spending more than 30% of income on housing, 2005	
	2000	2005	Percent change	Homeowners	Renters
Connecticut	$14,979	$12,490	-16.6%	88%	78%
Maine	$13,919	$11,539	-17.1%	71%	70%
Massachusetts	$12,774	$12,388	-3.0%	87%	73%
New Hampshire	$16,206	$15,981	-1.4%	82%	78%
Rhode Island	$11,178	$11,825	5.8%	87%	69%
Vermont	$12,774	$13,337	4.4%	80%	83%
New England	$13,368	$12,475	-6.7%	84%	74%
United States	$12,847	$12,459	-3.0%	80%	83%

Sources: Income data: author's calculations from the Current Population Survey. Housing data: NEPPC Working Paper 06-1, 2006; see the full report for details of the calculations.

For example, although the number of houses affordable for middle-income households was roughly twice the number of such households in most New England states, more than half of these units were occupied by higher-income households in 2004. Only by adding in affordable rental units can the housing demands of this group be met by the existing supply. But what does that leave for very low-income households? Excluding those apartments occupied by higher-income households, the ratio of the number of affordable apartments to the number of very low-income households ranged from one apartment for every 2.5 households in Massachusetts to one apartment for every four households in New Hampshire. This is not just a problem for New England—similar supply restrictions on very low-income households exist in the rest of the nation.

Table 2: In New England and the nation, the number of very low-income households exceeds the supply of available and affordable rental housing

	Number of very low-income households per affordable rental unit	Number of very low-income households per affordable and available rental unit
Connecticut	2.3	3.1
Maine	2.3	3.1
Massachusetts	2.0	2.5
New Hampshire	2.5	4.0
Rhode Island	2.1	2.7
Vermont	2.8	3.8
New England	2.2	2.8
United States	2.5	3.6

Source: NEPPC Working Paper 06-1, 2006. See report for full details of the calculations.

This inadequate supply of affordable rental housing for very low-income households is not entirely due to the choices of higher-income households.The supply of affordable housing potentially available to very low-income households (including those occupied by higher-income households) is inadequate even before considering the impact of crowding out. In 2005, there was only one such unit available for every 2.0 very low-income households in Massachusetts, and for every 2.8 households in Vermont.

The supply situation is not likely to improve soon. While many states in the region have had some success in building new affordable housing, they are also racing against the conversion of existing, affordable units. In recent years, many apartment owners have chosen to convert units to condominiums to take advantage of the hot real estate market. *The Greater Boston Housing Report Card 2005* found that nearly 1,200 rental units were converted to condominiums between 1999 and 2004; another 500 were converted in 2005. The report noted that many of these conversions occurred in working-class neighborhoods, where the new condo prices were not affordable to former occupants.

Even affordable housing with long-term use restrictions based on rent and tenant income limits are at risk of being converted to market-rate units as these restrictions expire—an attractive option in a strong real estate market. According to the National Housing Trust, New England states have lost more than 16,800 project-based, federally assisted units between 1995 and 2005. Other existing affordable units are at risk of becoming uninhabitable due to neglected maintenance.

While New England has a significant amount of new affordable housing in the pipeline, the amount of new affordable housing built in coming years is not likely to be sufficient to meet demand and to replace the number of existing affordable units that are scheduled to expire in the next decade.[4] Moreover, it is unlikely that the recent slowdown in the homeowner market will be deep enough or sustained enough to make a major dent in affordability, as prices have risen much more rapidly than incomes over the past decade. Even if prices fell sharply, the economic consequences associated with such a drop (e.g., a recession) would certainly further compromise the ability of the region's poor to pay for housing. There is no easy relief for this squeeze faced by the region's very low-income households. Tackling the problem requires a comprehensive strategy that addresses both sides of the equation by continuing to subsidize units while increasing and maintaining the supply of affordable housing.

Endnotes

[1] The exception is Maine, where the real income of middle-income households fell by 6.2 percent between 2000 and 2005. However, Maine's very low-income household income declined by 17 percent over the same period.

[2] Annual median household incomes are three-year moving averages calculated using the 2003-2005 Current Population Survey, where the head of household is above the age of 25 and not enrolled in school. Data are adjusted to real 2005 dollars using CPI-U.

[3] *The Greater Boston Housing Report Card 2003*.

[4] For example, in 2004 the U.S .Department of Housing and Urban Development (HUD) reported that of the 84,757 affordable units subsidized by HUD in Massachusetts, 10,642 have already been lost and 27,000 are at risk through 2010.

This policy brief is based on *The Lack of Affordable Housing in New England: How Big a Problem? Why Is It Growing? What Are We Doing about It?*, a New England Public Policy Center working paper. The full paper is available at http://www.bos.frb.org/economic/neppc/wp/2006/neppcwp0601.htm. To receive a copy of future policy briefs, please contact us at neppc@bos.frb.org or 617-973-4257.

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