Homeownership Policy at a Critical Juncture

Are Policymakers Overreacting to the Great Recession?

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The collapse of home prices and the dramatic increase in foreclosures have drawn calls to slow or stop promotion of homeownership, especially among low- and moderate-income families. Some commentators, like Richard Florida¹ and Dean Baker², see homeownership as overrated and suggest that public policies should shift from promoting homeownership to encouraging rental markets. If the stereotype before the Great Recession was that low-income families should own, the stereotype afterward has been that they should not. In many ways, this represents the worst of all worlds for these families: a “buy high, sell low, but don’t buy low” prescription that has been made independently of market conditions, much less the individual circumstances of each household. We suggest that homeownership has always been a viable policy for many but not all low-income families, because owning a home both adds to residential stability and is such an important source of saving and wealth accumulation.

Of course, the context matters greatly. Certainly, when home prices soared relative to rents and to incomes, it was a bad idea to encourage people to buy properties beyond their means in the hope that a price boom on top of recent price booms would later bail them—and their creditors—out. On the other hand, many families that purchased homes well before the Great Recession have come out ahead in terms of wealth and stability. Moreover, given current home prices and interest rates, homeowning has become unusually affordable. As recently as 2008, the median income family buying a home at the median value would have had to devote 18 percent of their income to their mortgage payment. As of late 2011, comparable payments were 35 percent lower—only 12.7 percent of income.³ Many Americans can now lock in monthly housing costs that are low relative to their incomes and to their current rent and not worry about the inevitable climb in rents over the next 30 years.

This brief reconsiders homeownership policies in light of recent changes in homeownership and home equity levels. The first step is to look at homeownership rates and the experience of homeowners over the last decade and through the Great Recession. How much of a decline in homeownership did groups with various educational attainment and different racial groups experience? Homeownership has long been the primary saving mechanism for low- and middle-income families. On average in these income groups, it exceeds the importance of bank accounts, retirement saving, and, of course, stock ownership.⁴ As homeowners pay off the principal on their mortgage loan and as inflation erodes the real value of their debt, they build up equity in their homes in an automatic way.

Did this continue over the last 10 to 12 years? The first part of this brief brings out new estimates of what happened to the housing wealth of middle-aged adults who had become homeowners by 1999. The second part examines future possibilities and risks for homeownership in light of current housing and credit market conditions. Does it still make sense financially to encourage homeownership, especially for some low- and middle-income families? The final section suggests a set

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of housing policies that are more efficient and more sensitive to market conditions than existing strategies.

**What Happened to Homeownership and Home Equity?**

The sharp declines in home prices during the years immediately following the Great Recession substantially lowered home equity, one of the two major sources of wealth for the middle class (the other is pension wealth). Many families with housing debts that exceeded the value of their homes continued paying their mortgages, but others did not keep up and often lost their homes to foreclosure or short sales. Given that millions of homeowners received foreclosure notices, homeownership rates were bound to decline.

In fact, homeownership rates—defined as the share of owner-occupied households out of all households—declined, but only about 3 percentage points. The decline looks modest in comparison to the number of foreclosure notices and the overall disruptions in the housing market. Data from the U.S. Census reveal that ownership peaked in 2004 at 69 percent (figure 1), fell to 68 percent by 2008, and then declined further to 66 percent by 2011. This change represents a 4 percent drop.

For blacks, however, the decline was a much larger 8 percent, falling from 49 to 45 percent. On the other hand, the percentage decline was only 3 percent for non-Hispanic whites. Married-couple households saw their homeownership rate fall from 84 to 82 percent (not shown).

**Patterns and Dynamics of Homeownership for Middle-Aged Americans**

Homeownership rates increase as people age and only decline slightly after age 75. Only 23 percent of people under 25 own homes, but the homeownership rate jumps to 58 percent when they reach their late 30s, 71 percent by their late 40s, and 78 percent by their late 50s. This brief focuses on homeownership for middle-aged Americans (30-49), those most likely affected by the collapse of home prices, between 1999 and 2011.

The analysis looks at homeownership from two perspectives. The first compares homeownership rates for specific age groups in 1999, 2007, 2009, and 2011. The second examines how homeownership evolved for a representative sample of heads of households in their 30s and 40s as of 1999, using longitudinal data drawn from the Panel Survey of Income Dynamics (PSID). By following the same individuals over time, we can observe flows into and out of homeownership. Did those who had become homeowners by 1999 manage to remain homeowners and to retain significant housing wealth after the onset of the Great Recession? What share of heads who were renters in 1999 subsequently managed to become and remain homeowners?

Comparisons of cohorts reveal declines in homeownership rates for most education and racial/ethnic groups of 30-39 year-olds and 40-49 year-olds, especially from 2007 through 2011. Regardless of year, homeownership rates are lower among less-educated and minority households, as would be expected for those with less average wealth and more unemployment. As figures 2 and 3 reveal, homeownership rates in 2011 were lower than homeownership rates in 1999, except for black heads in both age groups who had at least some college and for Hispanic heads in the 40-49 age group who had no college. In 1999, the homeownership rate of 30-39 year-old heads with no more than a high school diploma was 59 percent among non-Hispanic whites, 27 percent for blacks, and 49 percent for Hispanics. The sharp dropoff took place between 2007 and 2011, when homeownership rates dropped from 52 percent to 42 percent for these white non-Hispanic families, from 27 percent to 18 percent for black non-Hispanics, and from 50 percent to 45 percent for Hispanics. These changes are consistent with findings...
FIGURE 2. Homeownership Rate by Race, Ethnicity, and Education for Household Head Age 30–39


FIGURE 3. Homeownership Rate by Race, Ethnicity, and Education for Household Head Age 40–49

from a recent Urban Institute study showing that with the reduction in home prices, two-parent and Hispanic renters were more likely to become homeowners while blacks and single-parent families were less likely to do so.8

For heads in their 40s, homeownership levels are higher and generally decline less sharply. Over 2007–2011, less-educated whites in their 30s saw their homeownership rates fall from 52 to 42 percent while homeownership among less-educated whites in their 40s fell only 3 percentage points from 65 to 62 percent. For blacks in their 40s and with some college, homeownership rates actually increased from 40 to 52 percent. On the other hand, less-educated blacks experienced a decline in homeownership from 39 to 33 percent. Except for college-educated blacks and less-educated Hispanics, homeownership among 40–49 year-olds was lower in 2011 than in 1999.

Notwithstanding these cohort declines, heads who had become homeowners by their 30s or 40s may still have maintained their status as homeowners and even held on to some gains in housing wealth. Figure 4 provides the evidence on what happened to individuals who were homeowners in their 30s in 1999. It turns out that the vast majority of these initial homeowners were able to remain homeowners prior to and after the Great Recession. These individuals purchased homes well before the bubble burst after 2006. Many will have paid off a large share of their mortgage loans and most did not increase their borrowing substantially when home values and their home equity sharply increased. They were thus far less likely to be underwater on their mortgage. Still, racial and education disparities remain, with blacks and less-educated homeowners less likely to remain homeowners through 2011.

What about home equity? Certainly, the 2006–2011 decline in home prices reduced home equity substantially. However, the data reveal that for all groups owning homes, home equity was still far higher in 2009 than in 1999. Figure 5 tracks initial homeowners in 1999 who continued to own homes in 2007 and 2009, and displays their changes in home equity. Average home equity increased between 1999 and 2009 regardless of race and education. For example, black non-Hispanic heads with no more than a high school diploma saw their average home equity rise from $44,838 in 1999 to $75,616 in 2009. Median home equity also increased (not shown).

In summary, once longer periods are examined, the homeownership picture is quite mixed. On one hand, middle-aged heads of household today are less likely to own homes than families in the same age group 10 years ago. On the other hand, most families who bought homes 12 years ago managed to retain their status as homeowners and to sustain higher home equity levels than in 1999. In fact, at least for this period, the rates of return on home equity for those who remained homeowners far exceeded the returns these households would have earned had they placed their savings in the stock market. Overall, the findings support the idea that homeownership is still a strong tool for building assets, especially in the long run.

**New Opportunities for Homeownership**

Current credit and housing market conditions have become much more favorable for homeownership. The advantages are striking in terms of

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**FIGURE 4. Percentage Retaining Homeownership among Homeowners 30–39 in 1999**

lower housing costs, potential for building up equity, and avoiding future housing cost burdens that would derive from renting. Not only have home prices and interest rates declined but rents have already increased on average. Thus, while the Great Recession involved significant equity losses in the past, it also substantially lowered the cost of owner-occupied relative to rental housing. Today, a family earning the median income can buy a median-value home and spend only 15 percent of their income on mortgage payments (assuming a 5 percent down payment and a 4.5 percent interest rate). Even families far below the median income could finance a home with low monthly mortgage payments relative to annual income. For example, a household with a $30,000 income would have to devote only 19 percent of that income to pay the monthly mortgage on a home at the 25th percentile of home values.

In addition to lowering housing costs, homeownership allows families to build assets and not have to worry that rising rents will force them to move or bear continually higher cost burdens, assuming they take a fixed rate mortgage and property taxes do not go up rapidly. Indeed, the “real” mortgage out-of-pocket cost declines every year with inflation and compounds over time. The ability to increase home equity increases significantly as interest rates decline, because more of the monthly mortgage payment goes toward principal repayment and less toward interest. Consider a 4 percent, fixed rate, 30-year amortized mortgage in the context of zero inflation. In the very first month, 30 percent of the mortgage payment goes toward principal repayment and thus increases equity for the homeowner. Within two years, 3.6 percent of the mortgage would be paid off, implying $3,600 in accumulated assets on a $100,000 mortgage, even with no appreciation in home prices. By the beginning of the third year of the mortgage, over one-third of each month’s mortgage payment would represent savings going toward reducing mortgage debt. With inflation of 2 percent, the 4 percent interest rate translates into a real 2 percent rate and the asset component of monthly housing costs rises further.

Given the lessons from behavioral economics showing that simple and automatic approaches effectively increase savings, paying off a mortgage looks like an ideal instrument for low- and middle-income families to save consistently. Moreover, in many current situations, where monthly mortgage payments and other homeownership costs are less than rentals of comparable housing, homeownership can increase real incomes and the accumulated savings will generate wealth even if home prices do not rise.

In many geographic areas where rental markets are thin, homeownership also widens the range of housing choices. Limiting choices to rental markets prevents families from selecting locations they could afford if they obtain mortgage finance. Finally, homeownership with a fixed rate mortgage locks in most of the costs of housing. In contrast, renting exposes families to the risks of rental increases. It is true that declines in home prices can generate a capital loss, though those risks are less likely when the costs of owning versus renting are lower than when they are higher. For those likely to stay within a geographic region and, therefore, hold onto a house for a longer period of time, even capital losses are often only temporary paper losses.

New Challenges and Policy Remedies for Homeowners

Given today’s increasingly favorable market conditions, what policy measures hold promise for making homeownership viable for low- to moderate-income families? We describe three from a wide range of available options.

Expanding Homeownership Vouchers

The first—expanding homeownership vouchers—builds on the nation’s existing Housing Choice voucher system, a program that essentially provides vouchers low-income families can use to rent while paying no more than 30 percent of their income. The vouchers are equal to each local area’s fair market rent (FMR), generally designated as rent at the 40th percentile. Currently, the vouchers, along with other low-income housing subsidies, cover only about 30 percent of eligible families. Although the Housing Choice vouchers in theory can be used to finance homeownership, this option is rarely used, in part because of different administrative efforts involved and in part because administrators largely focused on rental housing have few incentives to favor this option. One proposal would simply make offering this option much clearer and more favorable for administrators.11

Another proposal is to create 1 million new homeownership vouchers similar to the Housing Choice vouchers but with modest adjustments.12 The vouchers would be restructured to homeownership and would be set at either the local FMR or the costs of homes at the 25th percentile (including interest, taxes, insurance, and a maintenance allowance), whichever is lower. Since the FMR is higher than these costs in nearly all metropolitan areas, the voucher value could be set lower than current vouchers. Some of the savings would pay for increased administrative resources to prepare families for homeownership, to inspect homes, and to help qualified participants obtain financing. Clearly, low-income families vary widely in their capacity to participate, and appropriate criteria must be developed.

Much of the homeownership voucher funding would act as insurance, since many of the eligible would often have incomes high enough so that their 30 percent contribution offsets nearly all the government voucher value. Consider providing a voucher to a family in Cleveland, Ohio, where the cost of a home at the 25th percentile is about $525 per month (including mortgage interest, taxes, insurance, and an amount set aside for maintenance). A family with someone earning $10 per hour, working 90 percent of the year, and receiving the earned income tax credit would have a high enough income to offset the full value of the voucher.

This approach differs sharply from past homeownership initiatives for low-income families, such as the expansion of credit through the subprime market. The past approach required low-income homeowners to pay very high interest rates with no government subsidies. Housing cost burdens for homeowners under this voucher plan would decrease significantly. Because the mortgage would be paid whether or not homeowners kept their jobs or received salary increases, the risks would be much lower, so interest rates could be kept lower too. Low-income owners who lost their jobs would not lose their homes as a result, since the income loss would simply lower their contributions and raise the government’s contribution, ensuring that the mortgage, taxes, and insurance are paid. Similarly, former policies encouraged families to abandon housing if it went even temporarily underwater, whereas under this program families could also lose the voucher itself and would have greater incentive to ride out market fluctuations longer.

The limited experience with the use of vouchers for homeownership shows the plan is feasible. Existing homeownership voucher programs have classes on mortgage loans, budgeting and saving, basic home maintenance, and foreclosure avoidance. In general, participants are eager to fulfill the requirements of employment and creditworthiness to become homeowners. Foreclosures are rare in existing homeownership voucher programs.13 Lubell and Cramer have also suggested Housing Choice Vouchers be used to build assets through an escrow account.14

Finally, as a temporary matter in recovery from a recession, homeowner vouchers would substantially increase the demand for owner-occupied dwellings. Hence, inventories of unsold homes would decline and prices would rise in many markets. These changes would benefit current homeowners and lower the losses other families, banks, and the federal government have been experiencing. Moreover, the initiative would reduce the waiting list for low-income housing assistance.

Modifying Tax Subsidies

In related work, we have shown how the current tax system favors homeownership among higher-income households and, once the effect on housing prices is taken into account, lowers the incentives for homeownership for low- and moderate-income households below what might be expected in a market without such subsidies.15 Such differentials are especially true in areas with land scarcity. In addition, the direct subsidies provided to lower-income renters but not owners further exacerbate the bias of the tax and spending systems against homeownership.

Our existing patchwork of federal housing subsidy programs currently provides tax subsidies to high-income households to own their homes while providing subsidies to low-income families to rent. In terms of promoting asset development, this is upside-down mobility policy.16

In a separate study, we offer alternative designs of tax subsidies for homeownership—converting some to a credit containing elements similar to the homeowner voucher approach suggested above.17 We suggest that the subsidy not be related to the amount of mortgage (a mistake we find in many proposals to change the deduction to a credit) but instead to homeownership itself, up to a cap. Supporting homeownership among low- and moderate-income families can be partly justified to offset the rent-oriented bias of transfer programs as well as distortions related to existing tax policy.
Expanding New Forms of Mortgages and Equity

The third policy option is shared equity homeownership programs, a new form of mortgage and equity building. These programs provide homeownership opportunities to income-eligible families that buy homes at below-market prices. In return for the subsidized purchase price, their potential capital gains when reselling the home are limited by resale restrictions.

There are relatively few rigorous evaluations of the benefits of shared equity homeownership programs. However, in one evaluation covering seven programs, researchers from the Urban Institute found that shared equity homeownership programs are effective in creating and preserving affordability for low- and moderate-income homeowners. Homeownership created by these programs also looks sustainable: only a few shared equity homeowners lost their homes to foreclosure, and over 91 percent of low-income, first-time homeowners remained homeowners five years after purchasing a shared equity home, much higher than the national norm of 50 percent. In addition, shared equity homeowners were able to resell their homes with the same frequency and for the same reasons as other homeowners. These outcomes were not related to the type of shared equity model (community land trust, deed restriction, or co-op). Of course, in any new design, it is crucial that the homeowner share significantly in the gains. By making homes more affordable to low-income families, these programs could promote sustainable homeownership for low- to moderate-income families in the future.

Concluding Comments

This brief examines whether encouraging homeownership is a sensible policy to help low-income and minority families obtain affordable housing and accumulate assets. Perhaps because of high unemployment or the tightening of credit standards, middle-aged heads are less likely to own homes today than they were a decade ago. Yet, even though home prices collapsed after 2006, homeownership has been a good investment for families that invested in earlier years. For example, families that bought their homes in 1999 experienced high returns on their investments and achieved high housing wealth through 2011. Current market conditions have again become more favorable for homeownership, with home prices low relative to rentals and mortgage interest rates near historic lows.

This brief takes a first step to examine the flows into and out of homeownership and gains in home equity over the past decade using the latest PSID data. Evaluating full benefits and costs of homeownership is far more complicated and merits rigorous future research. For example, evaluations on the effect of homeownership must also account for mortgage costs, the benefit of the mortgage income tax and property tax deduction, and the stream of implicit rents received from the home, as well as alternative costs of renting.

We acknowledge that homeownership might not be good for all families. For example, it might not be wise for currently unemployed and unstably employed families to purchase a home right away. Yet, many policy analyses are focusing too intensely on the losses faced by a specific cohort of homebuyers during the current recession, an emphasis that masks the opportunities afforded by current market conditions to families and to the government.

What policy options might be adopted to take advantage of today’s increasingly favorable market conditions for homeownership? We discuss three promising approaches to make homeownership viable for low- to middle-income families: expanding homeownership vouchers, modifying current housing tax subsidies, and expanding new forms of mortgages and equity. These are low-cost, potentially high-yield strategies with limited downside risk. Adopting some version of the three approaches would help not only the families that participate but the general economy as well.

Notes
3. These data come from the National Association of Realtors for January 2012, using a 4.37 interest rate, a home price of $163,000, a down payment of 20 percent of the home value, and an annual family income figure of about $61,000. See http://www.realtor.org/research/research/housinginx.
6. Ideally we would like to examine homeownership and home equity by how long a family has owned a home. As this information is not available from the PSID, we examine the flows in and out of homeownership over the years for which such data are available.
7. We do not present results from the subgroup of Hispanics with some college education, as the sample size is insufficient.
10. This example uses the American Community Survey tabulation for the home value at the 25th percentile in 2010 and then deflates the value by the observed 5 percent decline in home prices. See http://factfinder2.census.gov/faces/nav/jsf/pages/searchresults.xhtml?refresh=t.

13. This information is based on telephone interviews between the author and managers of programs using homeownership vouchers in Ohio and Michigan.


19. These seven programs include the Champlain Housing Trust in Burlington, Vermont; Northern Communities Land Trust in Duluth, Minnesota; Thistle Community Housing in Boulder, Colorado; the Dos Pinos Housing Cooperative in Davis, California; Wildwood Park Towne Houses in Atlanta, Georgia; A Regional Coalition for Housing in eastern King County, Washington; and the San Francisco Citywide Inclusionary Affordable Housing Program.

20. Based on three sites where data are available: 91.8 percent for Champlain Housing Trust (Burlington), 95.0 percent for Northern Communities Land Trust (Duluth), and 91.2 percent for Thistle Homes (Boulder).


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Given the chance, many low-income families can acquire assets and become more financially secure. Conservatives and liberals increasingly agree that government’s role in this transition requires going beyond traditional antipoverty programs to encourage savings, homeownership, private pensions, and microenterprise. The Urban Institute’s *Opportunity and Ownership Project* policy brief series presents some of our findings, analyses, and recommendations. The authors are grateful to the Annie E. Casey Foundation and the Ford Foundation for funding the policy briefs.