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A Path to Homeownership


Building a More Sustainable Strategy for Expanding Homeownership



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Homeownership continues to provide real social and economic benefits and remains a high priority for most American families, but the United States is experiencing significant declines in the ownership rate for the first time in decades. What we need is greater availability of targeted purchase assistance programs that address wealth barriers to homeownership.

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For more than 60 years, federal government efforts to expand homeownership were the centerpiece of U.S. housing policy. These policies made homeownership possible for the majority of American families. But the housing bust of 2007-2008 followed by the still-rolling foreclosure crisis in many parts of the country has sparked calls to reevaluate the importance of homeownership as a central policy goal of the federal government. Clearly, homeownership was oversold amid the recent housing bubble, and owning a home is not appropriate for every family. Yet homeownership continues to provide real social and economic benefits and remains a high priority for most American families.

What's needed, then, is a reevaluation of the ways in which the federal government encourages homeownership. Past racial discrimination in housing programs and access to credit results today in very uneven rates of homeownership between racial groups, which contributes even today to a wide and still-growing wealth gap in our country. Minority families and low-income families often find it difficult to come up with a sizable down payment for their first home precisely because they and their extended families lack the sufficient wealth. Expanding access to homeownership remains one crucial part of overcoming wealth inequality in our country. After all, even after the current deflation in home prices from inflated highs, the most valuable asset most Americans will ever own is their home.

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We have learned some important lessons from the foreclosure crisis. Most renters, of course, face multiple barriers to homeownership. Inadequate credit, lack of sufficient income, and other challenges may exist in addition to the lack of wealth or savings for a standard down payment. This is even more so the case with minority family renters, who lack parents and grandparents who own homes of their own and boast the financial capability to help their children and grandchildren with the down payments. Recent research consistently shows that wealth barriers pose the most significant obstacle to ownership for most of these low-income and minority families. As this paper will highlight, the lack of savings and family wealth can be addressed with carefully crafted programs.

Federal homeownership programs, however, have long focused primarily on credit and income barriers, and far too little on overcoming wealth barriers to homeownership. Depression era federal programs such as mortgage guarantees from the Federal Housing Administration and federal support for the mortgage securitization giants Fannie Mae and Freddie Mac focused on overcoming credit barriers. In the postwar era, these efforts succeeded in making homeownership possible for the great majority of American families. Between 1940 and 1965, the national ownership rate rose from 45 percent to more than 65 percent, but almost exclusively among white families due to widespread (and often legal) racial discrimination during this period.

But from 1965 to 1995 the homeownership rate remained virtually unchanged despite significant continued federal, state, and local investment in homeownership programs. Beginning in the late 1960s, a new set of programs focused on bringing down the cost of homeownership through mortgage interest rate subsidies. Federal mortgage revenue bonds, for example, allow states to fund mortgage loans at below market interest rates because interest earned by investors who buy

the bonds is exempt from federal income tax. But such programs have not had major impact on the homeownership rate because they do not overcome wealth barriers that prevent many renters from being able to afford a home.

Then, starting in the late 1990s, private mortgage market “innovation” led to further increases in the homeownership rate by lowering the amount of money required for a deposit on a home. Most of these loans artificially inflated the amounts borrowed through low “teaser” rates and other variations that masked the true borrowing burden. While some government-sponsored low down payment programs were combined with safer fixed-rate loans and prepurchase counseling, many of these mortgage products lacked basic consumer protections. We are now seeing that much of that growth was unsustainable because of unsound mortgage underwriting standards.

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Today, the United States is experiencing significant declines in the ownership rate for the first time in decades as first-time homeowners who were peddled subprime mortgages often with little or no down payment required but with hefty interest payments kicking in later. But the choice today is not between unsafe loans or low ownership rates for a large segment of the population. Instead, there are safer, proven strategies for making ownership possible for lower-income and minority buyers.

What we need is greater availability of targeted purchase assistance programs that address wealth barriers to homeownership. One-time purchase assistance—in the form of down payment assistance or neighborhood development subsidies that create below market-rate homes—expands the number of lower-income renters that can afford ownership dramatically. These kinds of purchase subsidies work because they both overcome the buyer’s lack of down payment savings and lower their monthly costs by reducing the size of the family’s mortgage. Especially promising are so called shared equity homeownership programs.

Shared equity homeownership programs make purchase subsidies cost-effective

A growing number of state and local housing agencies are pioneering the most dependable kind of home purchase assistance, shared equity homeownership programs. These programs invest significant upfront assistance to create homeownership units that remain affordable over the very long term and offer ownership to one generation of buyers after another. These programs structure public funding as investments rather than a grant to first-time homebuyers, making it possible for many more families to benefit from the same level of public investment. Frequently these first-time buyers save enough equity in their new homes to make subsequent home purchases, selling their first homes to new buyers through shared equity programs.

How does this work? State and local taxpayers who provide this funding make a fair deal with buyers who would otherwise be locked into renting as their only option. When investing in significant upfront purchase assistance, taxpayers expect these programs in return to pass the benefits of the investment along to another family. The terms of the deal require reselling the

home at a similarly affordable price, or in some cases repaying a share of any price appreciation back to the taxpayers through the agency that provided the subsidy.

Like any capital investment, investors expect a fair return on their investments. It should be no different for taxpayers as investors. In the private market, these returns on investment come in the form of cash profits. In the public realm, the deal between homeowners and taxpayers gives the homeowner the benefits of ownership and a reasonable amount of price appreciation. The public investor forgoes a cash return in exchange for keeping the home affordable for another homeowner when the first family leaves its starter home, in effect recycling a single investment multiple times.

Shared equity homeownership is not a new idea. Hundreds of local communities and several states have developed shared equity homeownership programs that have already created hundreds of thousands of permanently affordable homeownership units. There are currently 425,000 families living in limited equity housing cooperatives, many built with financing from now-defunct federal programs. There are more than 200 community land trusts in 42 states which have built or acquired more than 5,000 shared equity homes. And more recently, hundreds of inclusionary zoning and similar programs have created tens of thousands of price-restricted homes for low- or moderate-income households.

This is why a significant federal investment in a targeted purchase assistance program with an equity-sharing requirement would build a portfolio of affordable homeownership units. Over time, the portfolio would grow and help our nation overcome the persistent homeownership gap between low-income and minority families and other American homeowners.

Create a “Promote Affordability To Homeownership” fund

Current purchase subsidy programs are typically structured with only minimal ongoing affordability requirements. This means each new investment in affordable homeownership tends to serve only one family. By contrast, public investment in subsidized rental housing generally remains affordable over the long-term and serves one family after another. Consequently, an expanded home purchase subsidy approach, which requires a substantial initial investment, may appear relatively expensive.

Understood in context, however, purchase subsidies that lock in long-term affordable homeownership are relatively efficient. As a nation we already spend enormous sums of federal tax dollars annually to encourage ownership, while making little headway in expanding broadly affordable ownership. As noted in more detail below, the recently renewed homebuyer tax credit, for example, is expected to cost \$15 billion in 2009 alone, while most of the nearly 2 million taxpayers expected to claim the credit would have purchased a home without it. Some studies show only 200,000 of these buyers were truly new homebuyers for whom the credit made the difference, the cost per such buyer could be as high as \$75,000.

A PATH fund would provide both the short-term stimulus effects that come from increased home buying, and the long-term stabilization of neighborhoods and families that shared equity has already demonstrated.

Even without this special credit, the subsidy (in terms of lost tax revenues) to one higher-income family of the tax savings resulting from the mortgage interest deduction on a \$500,000 loan exceeds \$200,000 over the life of a 30-year mortgage. The barrier, then, is not a lack of budget resources currently available for subsidizing home ownership. But current subsidies are neither targeted to make the greatest difference in aiding families who could be owners but need some help, nor crafted to steward public investment for the longest possible public benefit.

The answer: Allocating even a small portion of current ownership subsidies to a Promote Affordability To Homeownership, or PATH, trust fund could easily finance a national shared equity homeownership program at a meaningful scale within a reasonable time frame.

Moreover, a PATH fund would provide both the short-term stimulus effects that come from increased home buying, and the long-term stabilization of neighborhoods and families that shared equity has already demonstrated. PATH assistance for working families who are otherwise qualified owners could stimulate the economy as effectively as a broad tax credit, but at a much lower cost. At an average public investment of \$25,000 per home, bringing roughly 200,000 new homebuyers into the market would cost \$5 billion.

A PATH fund of this magnitude structured as a shared equity investment rather than as a grant (like the home buying tax credit) could be expected to benefit families beyond the initial buyers. Experience shows that many of the lower-income and minority families who initially purchase a shared equity home later move up the housing ladder into the general market, making way for the next family in need. Consequently, a one-time investment of \$5 billion could make homeownership possible for between 600,000 and 1.5 million families over a 30-year period, based on typical rates of turnover, and depending upon size of initial subsidy.

Moreover, all (or nearly all) of these families would likely be families that would otherwise not have been able to purchase a home. The PATH program would target this assistance to buyers who are otherwise priced out of homeownership. Working with state housing agencies, the PATH fund would allow price and income limits that were responsive to regional markets rather than setting a single national limit. And importantly, because the shared equity feature requires the homeowner to give up a potential portion of future home appreciation, buyers who do not need help would have an economic incentive not to participate in such a program. This self-selecting feature would tend to tailor the program to those working families who see the best fit to their own circumstances. For buyers who lacked the assets to afford ownership otherwise, this public investment would make ownership attainable for the first time.

In short, shared equity purchase assistance is more carefully directed to where it is needed initially, and creates a long-term housing opportunity for multiple families. Overall, this is a far more efficient approach than what we do today. The pages that follow go into further detail on why the wealth side of the homeownership hurdle is the critical one to overcome, and how our shared equity proposal would work in practice. Examples from around the country will illustrate where programs such as these are working today—and working well. Policymakers therefore will find a path to continue to offer the opportunity of homeownership to every American who can afford to take that first step into their first home, while creating opportunities for the next generation of homeowners to follow in their footsteps.

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