Community Development Research Brief

Housing Market Recovery in the 12th District: *Implications for Low- and Moderate-Income Communities*

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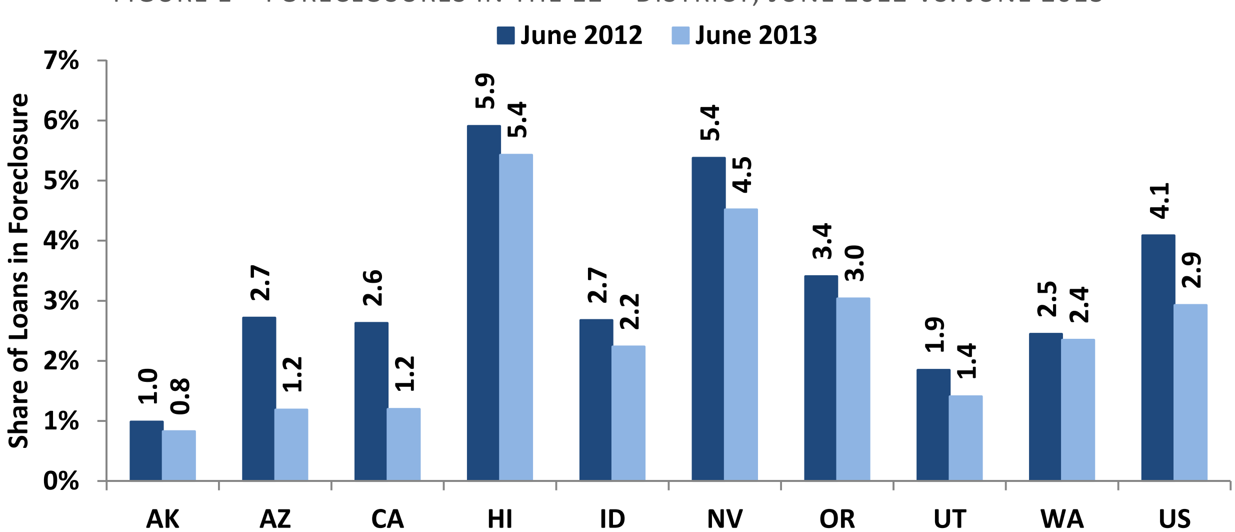
INTRODUCTION

Following the aftermath of the Great Recession, national indicators are starting to show signs of improvement in the housing market. Home prices increased by 11.9 percent in June 2013 compared to June 2012. [1] June 2013 also marks the 16th consecutive month of year-over-year home price gains.[2] Also, the number of properties that received a foreclosure filing in the U.S. was 14 percent lower for June 2013 than the previous month and 35 percent lower than the same time last year.[3] However, such robust indicators mask the realities of what's happening on the ground in low- and moderate-income (LMI) communities that were disproportionately affected by the housing crisis. Complicating matters is the unprecedented role of investors in the housing recovery and the changing nature of local housing markets.[4] There are pressing concerns around the potential impact of investor ownership on communities, tightening rental markets, and the ongoing challenges of preserving affordability for LMI households. This Research Brief provides an overview of these issues and examines housing market recovery and investor activity in the Federal Reserve's 12th District.

CURRENT CONDITIONS IN THE 12TH DISTRICT

As seen below in Figure 1, all 12th District states have seen a decrease in the foreclosure rate from June 2012 to June 2013 (for comparison, the rates at the national level were 4.1 percent in June 2012 and 2.9 percent in June 2013).[5] Among 12th District states, Hawaii and Nevada have the highest rates of foreclosure as of June 2013.

FIGURE 1 – FORECLOSURES IN THE 12TH DISTRICT, JUNE 2012 VS. JUNE 2013



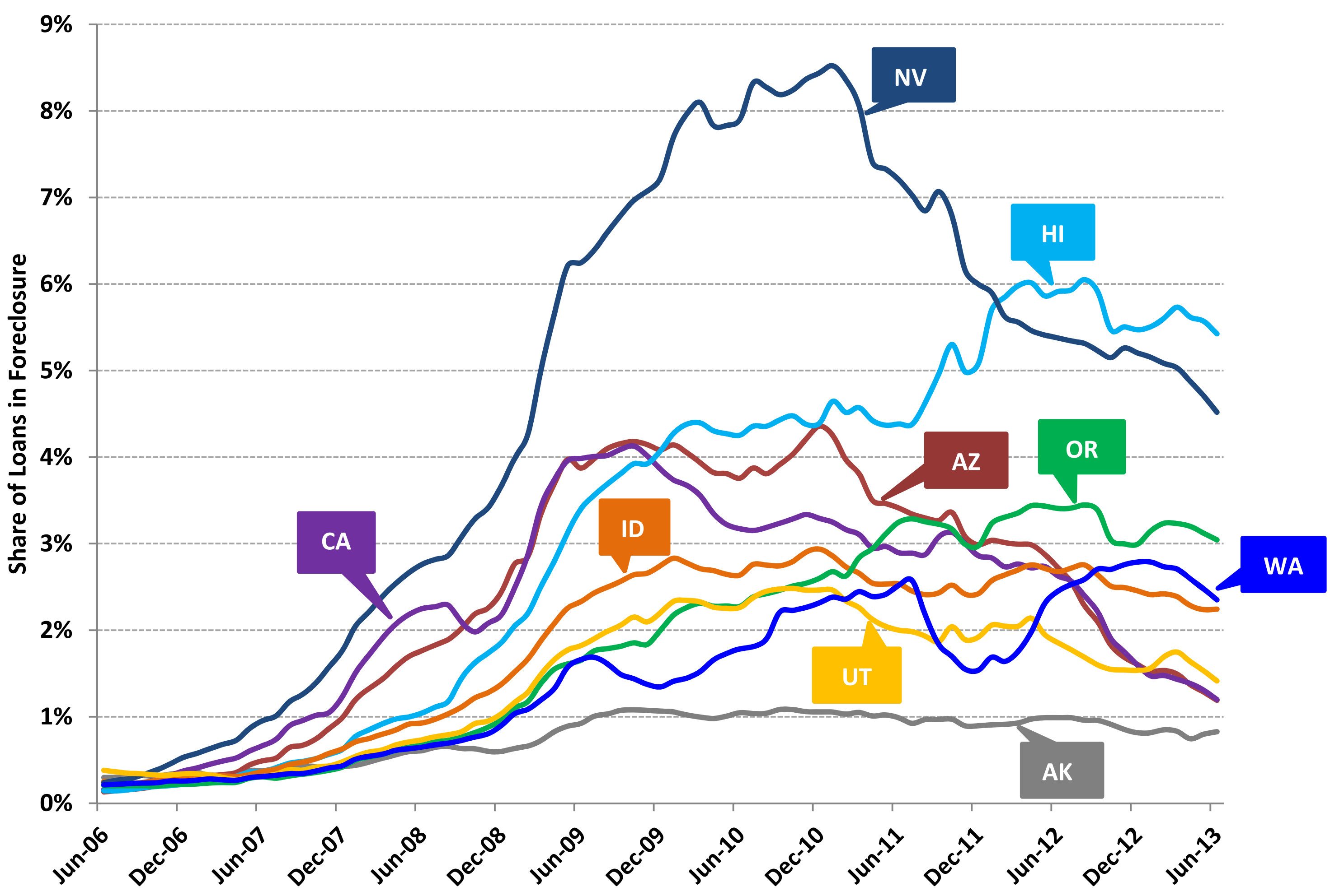
Source: LPS (Lender Processing Services Inc.) Applied analytics

[1] CoreLogic. Home Price Index Report, June 2013.
[2] Ibid.
[3] RealtyTrac. National Real Estate Trends & Market Info, Market Summary, June 2013.
[4] In February 2013, the Federal Reserve Board of Governors and the Federal Reserve Banks of Philadelphia and Cleveland hosted a conference entitled *Renters, Homeowners & Investors: The Changing Profile of Communities*. See http://www.federalreserve.gov/newsevents/conferences/renters-homeowners-investors-agenda.htm
[5] LPS (Lender Processing Services Inc.) Applied analytics, Mortgage Monitor Report, June 2012 and June 2013.

AN UNEVEN FORECLOSURE RECOVERY

While the above chart shows signs of improvement over the past year, Figure 2 provides a longer-term view, which reveals starkly different patterns of foreclosure recovery across 12th District states since the beginning of the crisis. Nevada, which was one the hardest hit states in the nation, saw a dramatic spike in the foreclosure rate, with a peak of 8.5 percent in January 2011. However, the state has since seen a fairly steady decline in recent years, with a foreclosure rate of 4.5 percent for June 2013. California and Arizona followed a more moderate peak and decline pattern over the years, with both states having a foreclosure rate of 1.2 percent for June 2013. In contrast, the foreclosure rates in Hawaii, Oregon and Washington have demonstrated slightly different patterns, showing peaks towards the end of 2012 and only recent signs of moderate declines. Utah saw a very moderate peak in late 2010, followed by a downward trend, while Alaska's foreclosure rate has held fairly steady around one percent since mid-2009, with a downward trend beginning in late 2012. Foreclosure recovery is uneven across the District at the state level and even greater variation is to be expected at the regional level (see Appendix for local trends at the county level).

FIGURE 2 – FORECLOSURE RATES IN THE 12TH DISTRICT, 2006 - 2013

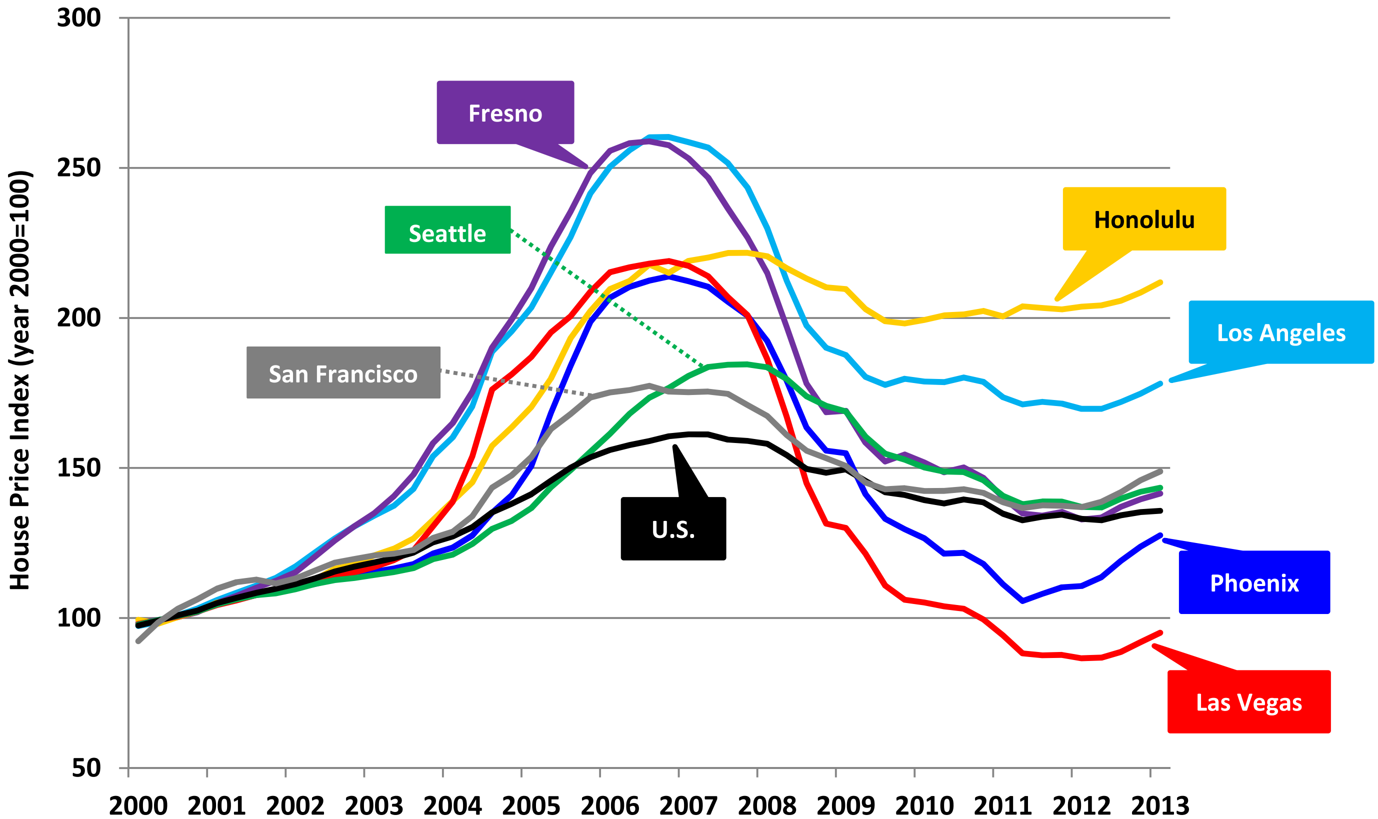


Source: LPS(Lender Processing Services Inc.) Applied Analytics

HOUSE PRICES

The 12th District saw dramatic price swings during the housing boom and bust. Figure 3 shows housing price trends in select MSAs from 2000 to 2013 (indexed to the year 2000). Fresno and Los Angeles both saw home prices increase by a factor of roughly 2.5 from 2000 to 2006, but by the first quarter of 2013, prices in Fresno were down 45.3 percent from the peak, while prices in Los Angeles were down 31.6 percent from the peak. The Las Vegas area saw some of the nation's steepest price declines and by late 2010, home prices in the area dropped below their values from the year 2000. Honolulu exhibited a slight decline from the peak in 2008, but compared to other MSAs in the district, home prices have remained resilient.

FIGURE 3 – HOUSE PRICES IN SELECT MSAS, 2000-2013



Source: Federal Housing Finance Agency (FHFA) House Price Index (Formerly called OFHEO House Price Index)

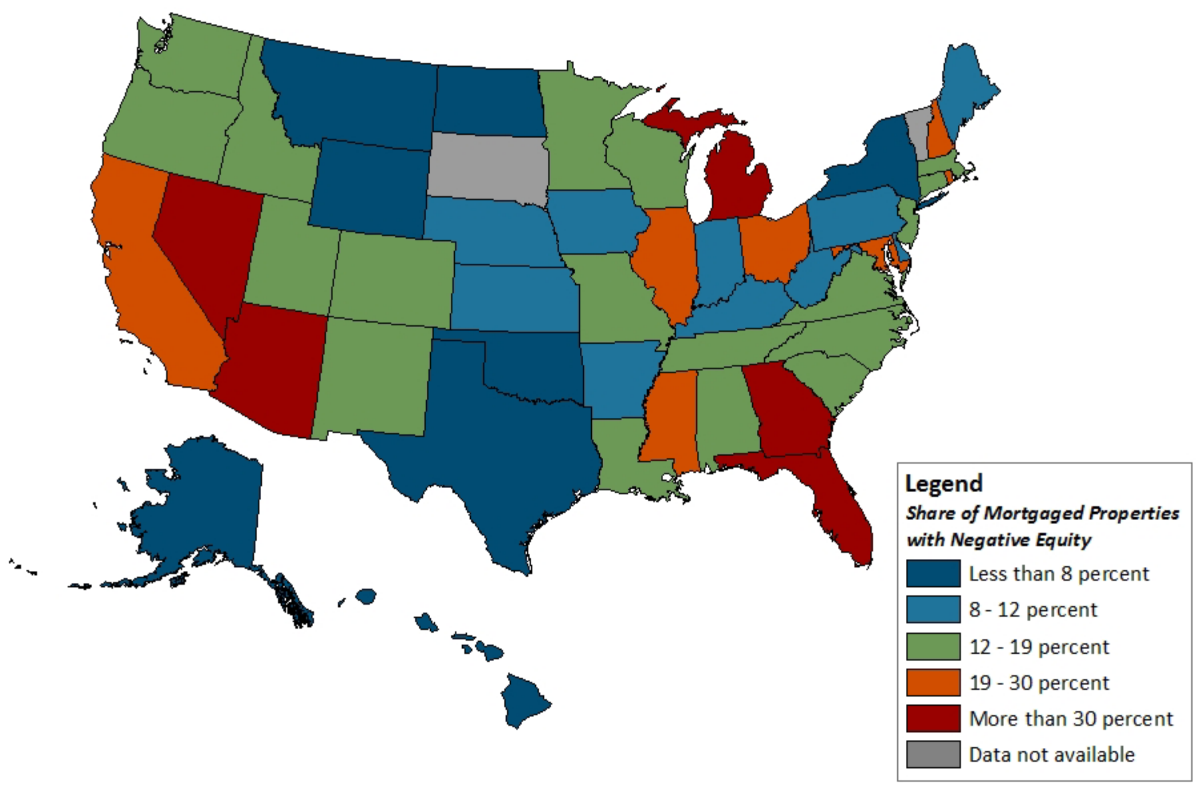
Across the District, prices generally flattened out between 2010 and 2011 and began to increase in 2012. Relatively stronger markets such as San Francisco and Seattle saw price gains of 8.7 percent and 4.7 percent, respectively, from Q1'2012 to Q1'2013. Hard-hit areas such as Phoenix and Las Vegas have seen strong gains, with prices in the first of quarter of 2013 roughly 15.3 percent and 9.9 percent higher, respectively, than the same time a year ago. Such rapid price increases in these troubled markets have led to concerns about the development of another housing bubble, particularly as other fundamentals such as jobs growth and incomes have not kept pace.[6]

[6] Scholer, K. (June 22, 2013) Housing Market: From Recovery to Bubble - Already? CNBC. http://www.cnbc.com/id/100834061

NEGATIVE EQUITY

Another important aspect of the housing market recovery is the extent to which homeowners have negative equity, meaning they owe more on a home than it is worth. Overall price increases, driven by strong demand for single family homes and limited available supply, are reducing the burdens of negative equity at the national level. According to CoreLogic, 850,000 residential properties nationally returned to positive equity during the first quarter of 2013, while 9.7 million residential properties with a mortgage remain in negative equity.[7] Figure 4 below shows the share of mortgaged residential properties with negative equity for the first quarter of 2013, with dramatic variations by state. For example, values range from a low of 5.6 percent in Montana to 45.4 percent in Nevada. High proportions of negative equity are particularly concerning for LMI communities, as negative equity tends to be concentrated at the lower end of the market. According to CoreLogic, in the third quarter of 2012, low- to mid-value homes (less than $200,000) had a negative equity share of 28.7 percent, almost twice that of borrowers with home values greater than $200,000, who had a negative equity share of 14.6 percent.[8] Additionally, research from the Department of Housing and Urban Development (HUD) suggests that negative equity is more likely to occur among households that are of color, younger, or have less than a high school degree.[9]

FIGURE 4 – NEGATIVE EQUITY BY STATE, FIRST QUARTER 2013



Source: CoreLogic Q1 2013

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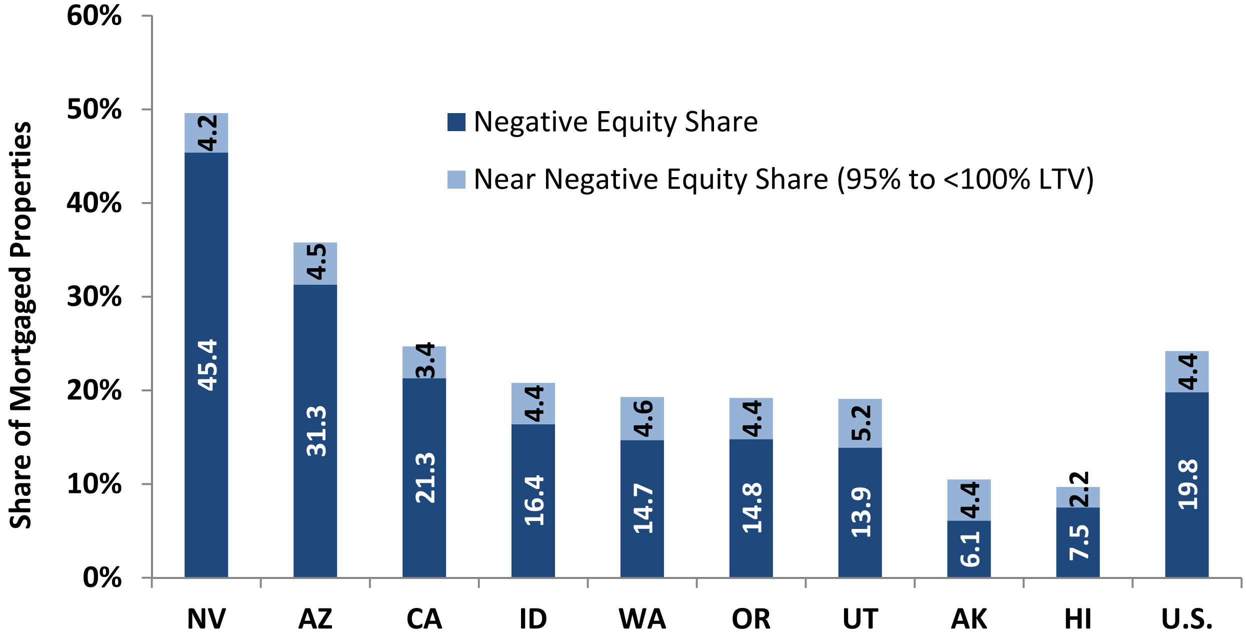
[7] CoreLogic, Q1 2013 Negative Equity Report

[8] CoreLogic, "Number of Residential Properties in Negative Equity Declines Again in Q3 2012." January 17, 2013.

[9] U.S. Department of Housing and Urban Development. Negative Equity in the United States, *PD&R Edge*. http://www.huduser.org/portal/pdredge/pdr_edge_research_072012.html

FIGURE 5 – NEGATIVE AND NEAR NEGATIVE EQUITY SHARE
12TH DISTRICT STATES, FIRST QUARTER 2013



Source: CoreLogic Q1 2013

Within the 12th District, negative and near negative equity (where loan to value ratios are between 95 and 100 percent) remain an issue (see Appendix for select data at the MSA level). As seen in Figure 5, Nevada, Arizona and California lead the District, with all three states having a combined negative or near negative equity share greater than the national average. While all District states saw an improvement in negative or near negative equity from the fourth quarter of 2012 to the first quarter of 2013,[10] far too many households remain vulnerable to another downturn in the housing market.

FIGURE 6 – AVERAGE LOAN TO VALUE RATIOS

State	Average LTV
Nevada	96.0%
Arizona	79.1%
Idaho	69.8%
Utah	67.7%
Oregon	67.0%
Alaska	66.2%
Washington	65.4%
California	63.4%
Hawaii	50.7%
U.S.	***67.2%***

Source: CoreLogic Q1 2013

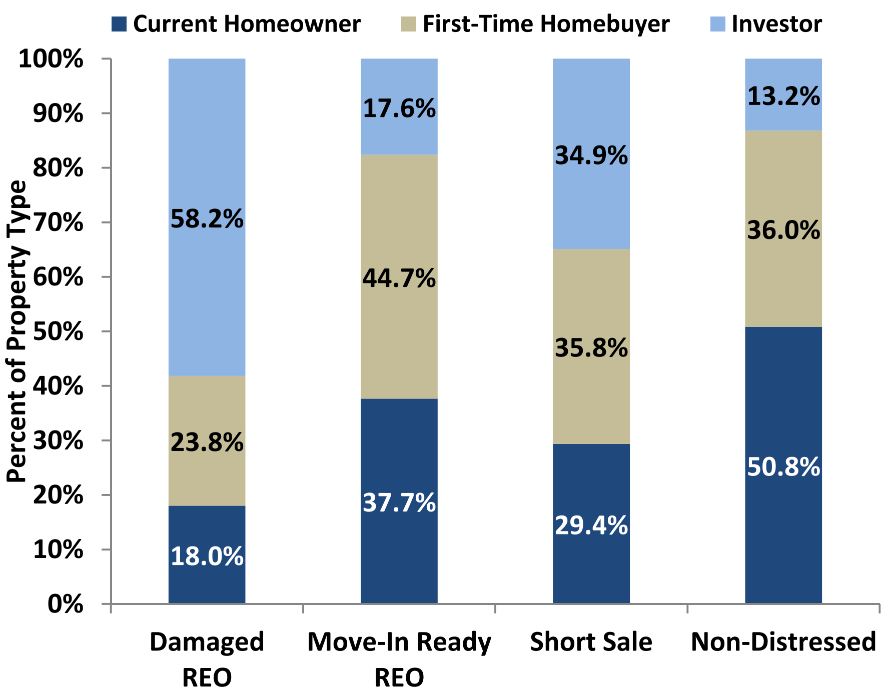
Homeowners in the 12th District remain relatively highly leveraged, as shown in Figure 6. Nevada, Arizona, Idaho, and Utah all have average Loan to Value (LTV) ratios above the national average of 67.2 percent, with Nevada having the highest average LTV in the country, at 96.0 percent. Limited equity and high LTV ratios make it extremely difficult for homeowners to refinance and take advantage of lower interest rates, which has prompted the development of Federal efforts such as the Home Affordable Refinance Program (HARP). In addition, recent research suggests that highly leveraged homeowners reduced consumption more than other owners, despite having smaller changes in net worth, suggesting that overleveraging may be a factor in the slow economic recovery.[11]

[10] CoreLogic, Q1 2013 and Q4 2012 Negative Equity Report
[11] Dynan, Karen. The U.S. Household Debt Overhang. *Brookings Papers on Economic Activity*, Spring 2012.

INVESTOR ACTIVITY

Low prices and increased demand for rental properties drew investors to purchase single family homes in markets across the country, particularly in areas with high concentrations of distressed properties. As seen in Figure 7, in June 2013, investors purchased 58.2 percent of damaged REO properties and 34.9 percent of short sales, compared to just 17.6 percent of move-in ready REOs and 13.2 percent of non-distressed properties.[12] There have been concerns that investor purchases (often made as all-cash offers) are crowding out qualified homebuyers who, despite having adequate income and access to mortgage credit, are unable to enter the market. According to RealtyTrac, all-cash purchases accounted for 30 percent of all sales in June 2013 nationally, while institutional investor purchases (sales to non-lending entities that purchased at least 10 properties in the last 12 months) accounted for 9 percent of all residential sales.[13] States with the highest percentage of institutional investor sales included Georgia (23 percent), Nevada (16 percent), Arizona (15 percent), and Oklahoma (13 percent).[14] Additionally, investors (of any size, not just institutional investors) accounted for 19.7 percent of buy-side transactions for the month of June 2013, while current homeowners made up 44.6 percent and first-time homebuyers made up 35.7 percent.[15]

FIGURE 7 – WHO IS BUYING PROPERTIES NATIONWIDE? JUNE 2013



Note: 3-month moving average. Source: Campbell/Inside Mortgage Finance

But recent data from a national survey of real estate agents suggests that investor activity may be slowing down. In June 2013, the investor share of home purchase transactions fell to 19.7 percent, the lowest level recorded since September of 2012.[16] Survey respondents attributed the ongoing decline in investor activity to rising home prices and less opportunity for investors to flip homes, particularly in hot markets around the country. Another factor in the decline in investor activity is the rapidly shrinking supply of distressed properties; the percentage of home purchases involving foreclosures or short sales fell to 28.2 percent in June, a sharp decline from the 40.3 percent level recorded a year earlier.[17]

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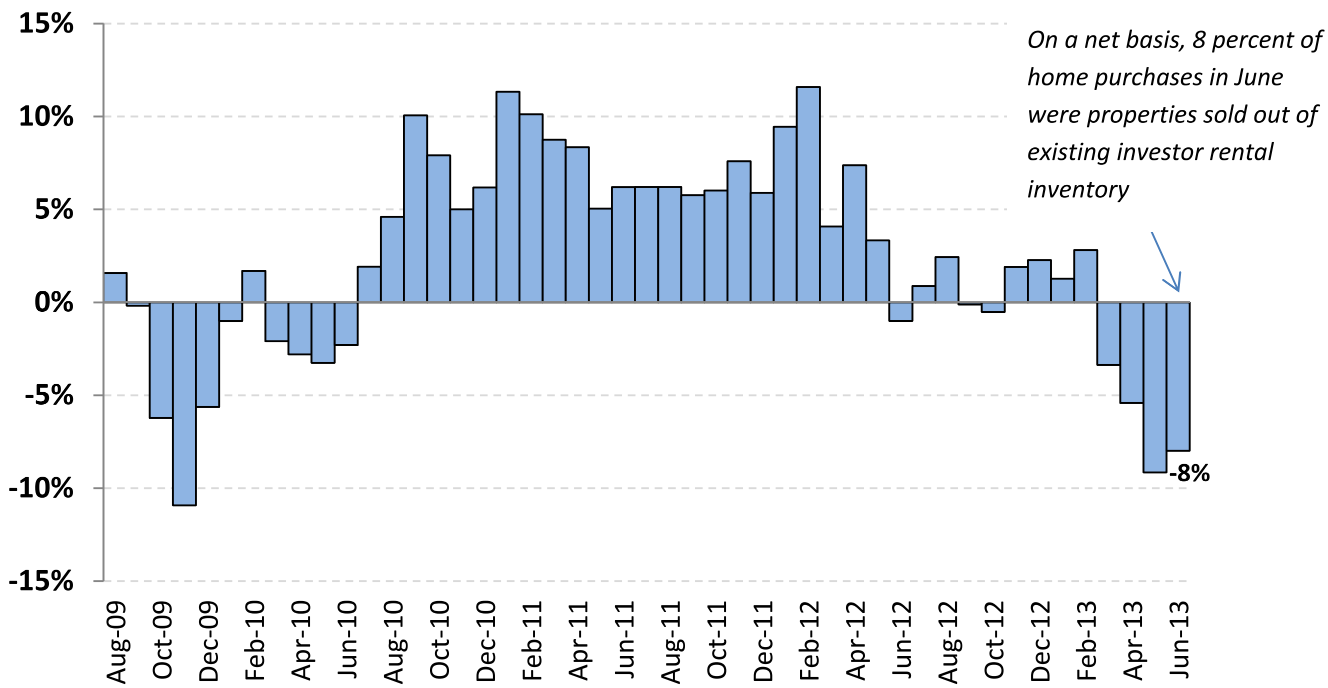
[12] Campbell/Inside Mortgage Finance HousingPulse Tracking Survey (June 2013).
[13] RealtyTrac. "All-Cash and Institutional Investor Purchases Down from Year Ago in June But Short Sales Continue to Increase." July 23, 2013.
[14] Ibid.
[15] Campbell/Inside Mortgage Finance. HousingPulse Tracking Survey (June 2013).
[16] Campbell/Inside Mortgage Finance. "Current Homeowners Drive Home Purchase Market in June As Investors Continue to Lose Steam, HousingPulse Shows." Press release, July 22, 2013.
[17] Ibid.

In addition, investors appear to be selling off existing rental inventory, as shown in Figure 8 below. “Net investor absorption” reflects the extent to which investors are adding or releasing properties out of their inventory. For June 2013, on a net basis, eight percent of home purchases were properties sold out of existing investor rental inventory.[18] This is in contrast to activity from late 2010 through mid-2012, when on a net basis, roughly five to ten percent of home purchases were being added to investor inventories.

FIGURE 8 – ESTIMATED NET INVESTOR ABSORPTION



Note: 3-month moving average. Net investor home purchasing estimated by subtracting the percent of first time homebuyers from the percent of distressed property sales. Current homeowner transactions are not included as they typically buy and sell a home at the same time. Source: Campbell/Inside Mortgage Finance.

This is not to suggest that the issue of investor purchases is diminishing. The largest institutional investor, Blackstone Group, LP has spent more than $5.5 billion to acquire roughly 32,000 rental homes in the past year.[19] The second largest investor, California-based American Homes 4 Rent, owns or controls roughly 19,000 homes and announced its initial public offering on July 31, 2013, making it the third single-family home-rental real estate investment trust (REIT) to go public. However, weak early performance of these stocks has prompted two other prominent investors, Colony American Homes and Waypoint Homes to postpone their plans to go public.[20] It remains to be seen whether these companies can build an institutional real estate class from U.S. single-family rental homes and what the potential implications would be for communities across the country.

[18] Campbell/Inside Mortgage Finance HousingPulse Tracking Survey (June 2013).
[19] Wheelan, R. & Demos, T. (July 30, 2013). Single-Family Rental Firm's IPO to Test Market. *The Wall Street Journal.*
[20] Ibid.

Robust data on investor activity is difficult to obtain, particularly at the local level, but it's clear that the nature of investor activity varies by geography. Figure 9 provides a snapshot of investor activity for select markets in the District for the month of June 2013. The share of all homes purchased by absentee buyers (mostly investors) ranges from 21.6 percent in Seattle, Washington to 50.7 percent in Las Vegas, Nevada. Similarly, the share of all homes bought in cash ranges from 22.8 percent in Seattle to 60.1 percent in Las Vegas. The table also shows the variation in home prices across the District, with absentee buyers paying a median price of $138,000 in Phoenix, while absentee buyers in the Bay Area and Southern region of California paid a median price of $405,000 and $300,000 respectively.

FIGURE 9 – INVESTOR ACTIVITY, JUNE 2013

Market	Homes purchased by absentee buyers	Median price paid by absentee buyers	Share of all homes bought in cash
Seattle, WA	21.6%	$249,000	22.8%
Bay Area CA	23.7%	$405,000	25.6%
Portland, OR	28.0%	$221,000	23.4%
Southern CA	28.7%	$300,000	30.2%
Phoenix, AZ	38.2%	$138,000	40.2%
Las Vegas, NV	50.7%	$145,000	60.1%

Source: DataQuick, June home sales reports.

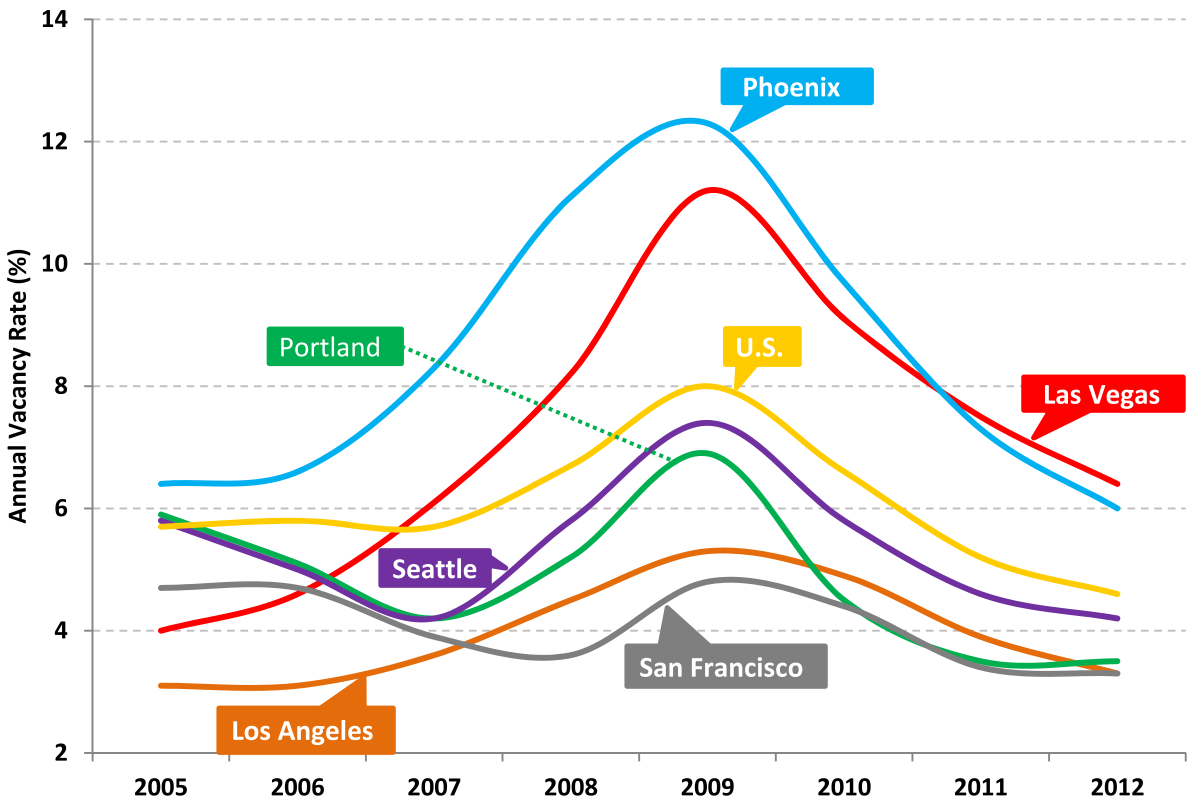
Large-scale investors have been most active in hard-hit markets such as Phoenix, Las Vegas and parts of California, which have had ample distressed inventory and increasing rental demand. For example, an analysis by the Urban Strategies Council finds that as of October 2011, investors had acquired 42 percent of all properties that went through foreclosure since 2007 in Oakland, California; of these investor acquisitions, 93 percent are located in low-income neighborhoods of the city. Additionally, only ten out of the top 30 most active investors are located in Oakland.[21] The Urban Strategies Council report also states that increases in non-local ownership and non-owner occupied housing raise concerns about the extraction of wealth from low-income neighborhoods, shifting tenure, neighborhood succession, and the displacement of residents.

RENTAL MARKETS

Another growing concern for LMI communities is the tightening of rental markets, as most lower-income households are renters, rather than homeowners. The wave of foreclosures that spread across the country displaced numerous households (both owners and renters whose landlords were foreclosed upon), increasing the demand for rental units. Nationally, apartment vacancy rates have fallen from a high of 8.0 percent in 2009 to 4.6 percent for 2012 (see Figure 10).[22] A vacancy rate of five percent is generally considered to achieve a balance between the interests of landlords and tenants. Phoenix and Las Vegas saw some of the District's highest vacancy rates, peaking at 12.3 percent and 11.2 percent, respectively, in 2009. As of 2012, vacancy rates had fallen to 6.4 percent in Phoenix and 6.0 percent in Las Vegas. Other metro areas in the District generally have lower vacancy rates compared to the national average. For example, in the Pacific Northwest, Portland and Seattle had 2012 vacancy rates of 3.5 percent and 4.2 percent, respectively, while in California, Los Angeles and San Francisco had among the lowest vacancy rates, at 3.3 percent for both metros in 2012.

[21] Urban Strategies Council. Who Owns Your Neighborhood? The Role of Investors in Post-Foreclosure Oakland. June 2012.
[22] All apartment vacancy data comes from REIS Apartment Metro Reports.

FIGURE 10 – ANNUAL VACANCY RATES FOR SELECT METROS, 2005-2012



Source: REIS, Apartment Market Reports

In addition to fewer available units, LMI households must also contend with rising rents. As shown in Figure 11, the average asking rents for many major metro areas in the District have steadily increased over the past few years.[23] The average rent in Seattle went from $1,047 in the second quarter of 2011 to $1,150 in the second quarter of 2013, an increase of 9.8 percent. San Francisco, which is one of the highest cost markets in the nation, had an average asking rent of $2,070 for the second quarter of 2013, a 9.6 percent increase from two years ago. However, even in lower cost markets, such as Phoenix and Las Vegas, asking rents have increased.

FIGURE 11 – AVERAGE ASKING RENTS FOR SELECT METROS

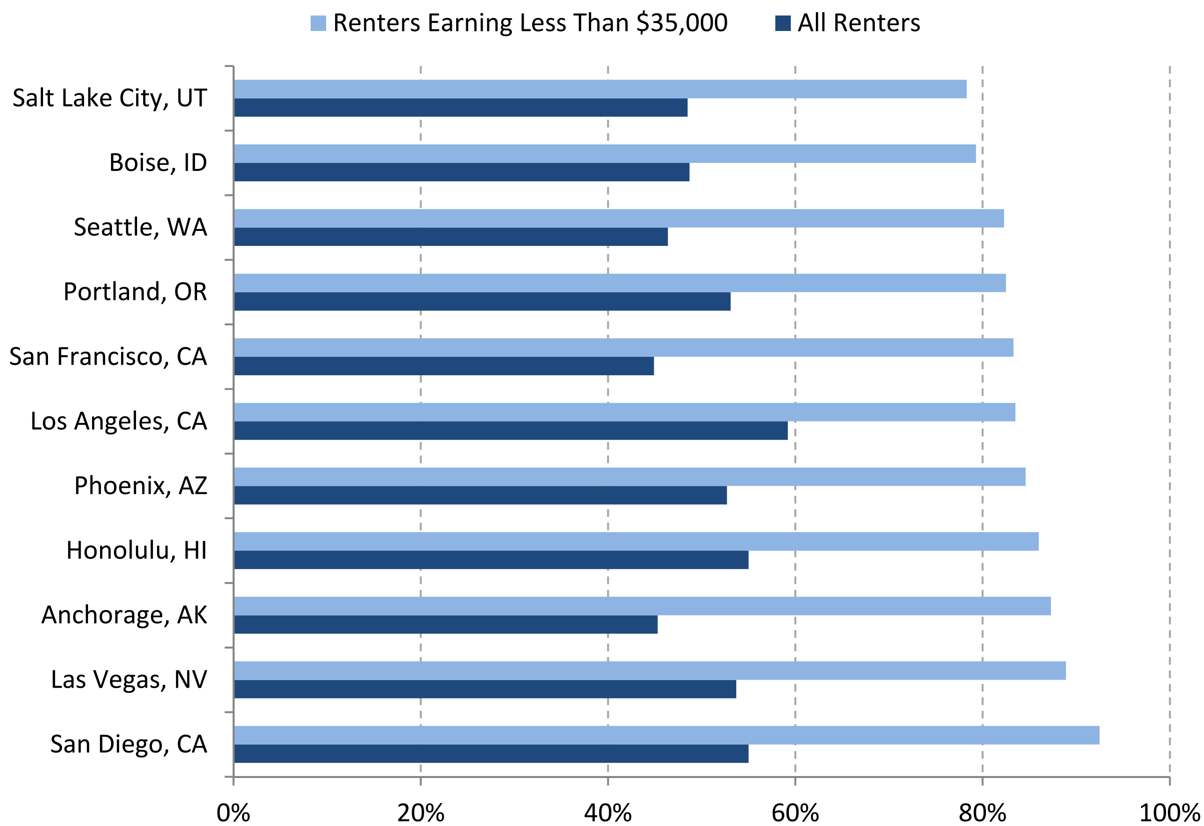
Metro Area	2011 Q2	2012 Q2	2013 Q2	% Change (Q2'11 vs. Q2'13)
Seattle, WA	$1,047	$1,085	$1,150	9.8%
San Francisco, CA	$1,888	$1,991	$2,070	9.6%
Portland, OR	$849	$871	$905	6.6%
Salt Lake City, UT	$755	$777	$797	5.6%
Los Angeles, CA	$1,402	$1,435	$1,472	5.0%
Phoenix, AZ	$758	$774	$790	4.2%
Las Vegas, NV	$805	$819	$836	3.9%

Source: REIS, Apartment Market Reports

[23] Note: Admittedly, average rent is not an ideal statistic since luxury rentals in higher-end markets such as San Francisco and Seattle skew the average upwards, as compared to median rents. However, up to date median rental data at the metro level is very difficult to obtain.

Rental affordability remains a major concern for LMI communities. Despite broader signs of economic recovery, such as decreasing unemployment rates and reports of increased hiring, many lower-income households still struggle to make a living wage and find adequate housing that fits within their budget.[24] Figure 12 below shows the share of renter households spending more than 30 percent of household income on rent (families who pay more than 30 percent of their income for housing are considered cost burdened).[25] Between 45 percent and 60 percent of all renters across multiple metro areas in the District are housing cost burdened. However, the share of renters that are housing cost burdened increases dramatically among renters earning less than $35,000 annually. For example, in Las Vegas and San Diego, 88.9 percent and 92.5 percent of renters earning less than $35,000 are paying rents that are considered unaffordable.

FIGURE 12 – HOUSEHOLDS PAYING MORE THAN 30% OF INCOME FOR HOUSING COSTS



Source: U.S. Census Bureau, American Community Survey, 2011 5-year estimates

[24] See the Federal Reserve Bank of San Francisco's *Vantage Point: The 12th District Community Indicators Project* for more details. Available at http://www.frbsf.org/community-development/publications/vantage-point/

[25] U.S. Department of Housing and Urban Development, *Affordable Housing*, available from http://portal.hud.gov/hudportal/HUD?src=/program_offices/comm_planning/affordablehousing/

CONCLUSION

Recovery in local housing markets, while desperately needed, has also presented the community development field with a number of challenges. Numerous questions remain about the impact that investor activity will have on communities, particularly in areas such as Oakland, Phoenix and Las Vegas that have seen heavy investor purchases. Major concerns surround the ability and willingness of absentee owners to invest in and maintain properties, with LMI renters bearing the burden. Additionally, investors adopt different strategies depending on local factors, such as flipping homes for quick resale or holding homes to rent out over the medium to long term, each of which will likely have different implications for local neighborhoods.[26] All of this uncertainty creates particular challenges for LMI households and communities, which often lack the financial and political resources to mitigate risk and advocate for appropriate protections.

This is not to suggest that all investors are alike, or that any and all investor activity will be detrimental to communities. Investors differ in their skill, resources, and priorities, and there may be important opportunities for the community development field to partner with and learn from them. For example, many investors will be experimenting with scattered-site single-family rental property management (an issue which has posed numerous challenges for non-profit housing developers) creating opportunities for improvement and innovation. Similarly, direct partnerships may also form in an effort to support local communities. For example, Waypoint Homes and Enterprise Community Partners announced a partnership in 2012 to purchase, renovate, and lease up to 100 single-family homes in distressed neighborhoods in Oakland, CA. Waypoint will serve as the general operating partner and will assess acquisition targets, complete the rehab and manage the properties. Enterprise will coordinate the tenant financial education and the workforce development component at the construction sites and will also serve as liaison with local government representatives and local nonprofit groups.[27]

Given the wide-range of housing recovery issues across the District, it is imperative that strong public policies play a role in promoting neighborhood stabilization and protecting LMI households and communities. For example, a number of cities have adopted rental registries to collect data on rental properties and owners, which allows for better code enforcement and improved property maintenance. Other cities have implemented foreclosed property registries to manage blight and monitor properties through various stages of delinquency. Other approaches, such as policies that promote land banking or community land trusts, can help sustain local property ownership. In addition, efforts such as the National Community Stabilization Trust's First Look program allows municipalities and locally based housing providers to gain access to foreclosed and abandoned properties in targeted neighborhoods, without facing competition from investors, in a more streamlined and predictable manner that saves valuable time and resources.[28] Just as each market is unique, the appropriate policy response will vary by community.

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[26] For more on investor typology, see Immergluck, D. The Role of Investors in the Single-Family Market in Distressed Neighborhoods: The Case of Atlanta. Joint Center for Housing Studies, February 2013.

[27] PR Newswire. Enterprise and Waypoint Homes Announce $20 Million Housing Recovery Partnership for Oakland, CA. June 8, 2012. http://www.prnewswire.com/news-releases/enterprise-and-waypoint-homes-announce-20-million-housing-recovery-partnership-for-oakland-ca-158085645.html

[28] National Community Stabilization Trust. Property Acquisition: First Look. http://www.stabilizationtrust.com/programs_services/property_acquisition/first_look/

Additionally, serious funding constraints for affordable housing development continue to pose challenges for maintaining affordability for LMI households. Reductions in funding at all levels of government represent the new reality that many jurisdictions and developers must contend with, suggesting that new models and new funding sources must be explored. For example, housing developers can consider models that connect affordable housing to health and healthcare, such as the Healthy Futures Fund (HFF). This new investment vehicle, developed by the Local Initiatives Support Corporation (LISC) in partnership with Morgan Stanley and the Kresge Foundation is bringing together grant, loan and equity capital to build affordable housing and community health centers as well as fund services that link them in places where one of the two already exist. [29]

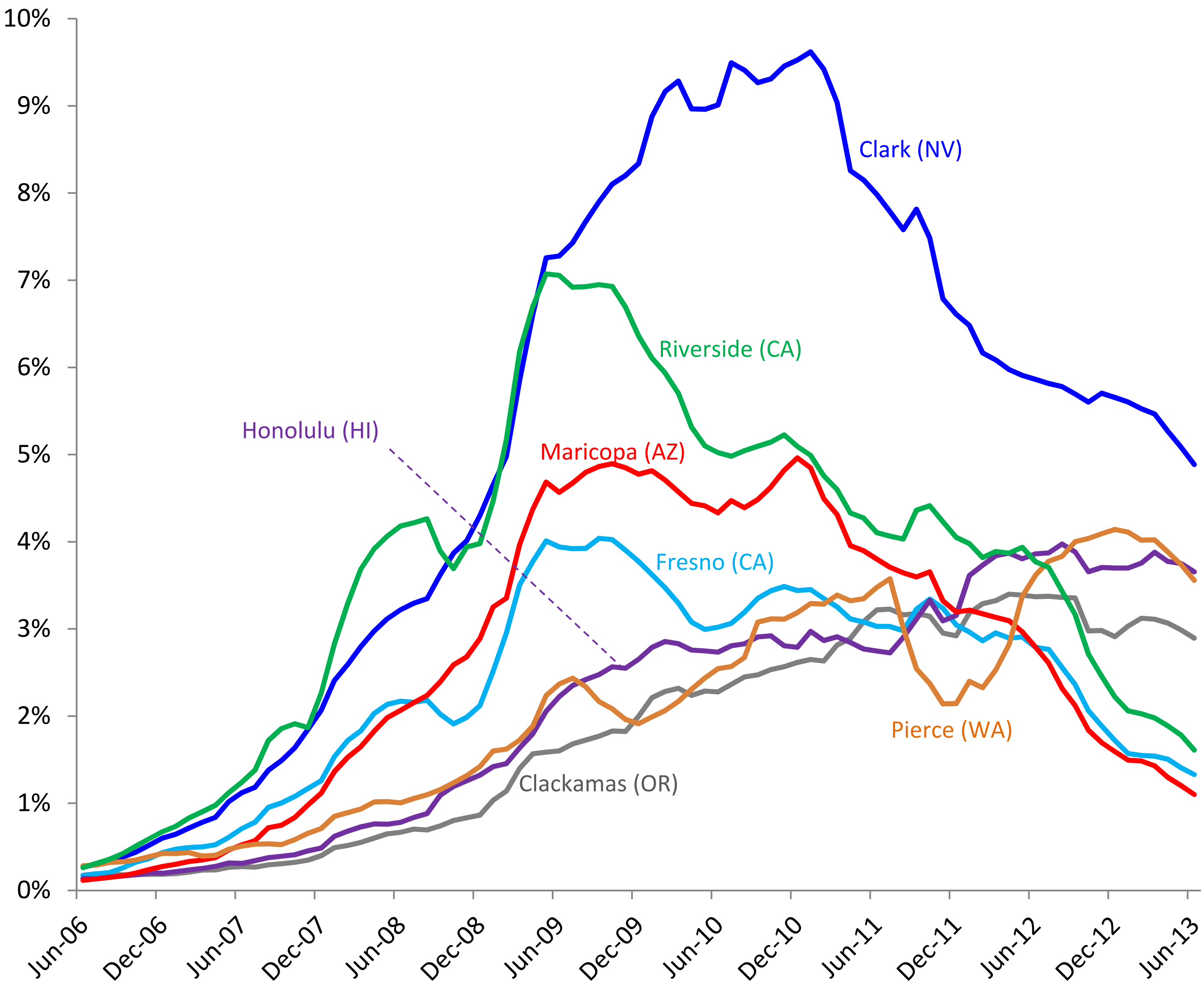
Across the multiple aspects of housing market recovery, success will ultimately lie in the ability of local players to partner in meaningful ways and develop a coordinated response to local challenges. As the field considers "what works" in community development, it must continue to advocate for strong policies that support the recovery and long-term sustainability of LMI communities across the country.[30]

[29] Boes, K. (2013). Connecting Housing and Health Care through Community Development. *Community Investments*, Vol. 25, Issue 1. Available at http://www.frbsf.org/community-development/files/Boes_CISP13.pdf

[30] For more information, see *Investing in What Works for America's Communities*. Eds. Nancy Andrews, et al. San Francisco: Federal Reserve Bank of San Francisco and Low Income Investment Fund, 2012. http://www.whatworksforamerica.org/

APPENDIX

FORECLOSURE RATES FOR SELECT COUNTIES, 2006-2013



Source: LPS(Lender Processing Services Inc.) Applied Analytics

NEGATIVE EQUITY BY SELECT CORE BASED STATISTICAL AREAS (CBSA), Q1 2013

Core Based Statistical Area	Average LTV	LTV Share >0 to <80%	LTV Share 80% to <100%	Negative Equity Share	Near Negative Equity Share (95% to <100% LTV)
Santa Ana-Anaheim-Irvine, CA	58.5%	73.0%	15.9%	11.1%	2.9%
Portland-Vancouver-Hillsboro, OR-WA	65.5%	63.4%	24.9%	11.7%	4.2%
Seattle-Bellevue-Everett, WA	61.8%	65.6%	21.5%	12.9%	3.9%
Los Angeles-Long Beach-Glendale, CA	59.2%	67.0%	16.8%	16.2%	2.9%
San Diego-Carlsbad-San Marcos, CA	64.6%	60.5%	20.0%	19.5%	4.0%
Oakland-Fremont-Hayward, CA	65.9%	60.9%	16.5%	22.6%	3.3%
Sacramento-Arden-Arcade-Roseville, CA	75.3%	53.0%	21.2%	25.8%	3.8%
Riverside-San Bernardino-Ontario, CA	83.2%	45.8%	22.8%	31.4%	3.7%
Phoenix-Mesa-Glendale, AZ	80.4%	44.8%	22.6%	32.5%	4.3%

Source: CoreLogic Q1 2013 Negative Equity Report