THE STATE OF THE NATION’S HOUSING 2019
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Continuing Shortfall in Supply

Just as the recent housing downturn was longer and deeper than any other since the Great Depression, the residential construction rebound has been slower. Since reaching bottom in 2011 at just 633,000 new units, additions to the housing stock have grown at an average annual rate of just 10 percent. Despite these steady gains, completions and placements totaled only 1.2 million units last year—the lowest annual production, excluding 2008–2018, going back to 1982.

The sluggish construction recovery is in part a response to persistently weak household growth after the recession. On a three-year trailing basis, the number of net new households dropped below 1.0 million in 2008 and held below that mark for seven straight years, including a low of just 534,000 in 2009. By comparison, even through the three recessions and large demographic shifts that occurred between 1980 and 2007, household growth still averaged 1.3 million annually and only dipped below 1.0 million once.

With the economy finally back on track, household growth picked up to 1.2 million a year in 2016–2018, close to expected levels given the size and age composition of the population. But new construction was still depressed relative to demand, with additions to supply just keeping pace with the number of new households (Figure 1). As a result, the national vacancy rate for both owner-occupied and rental units fell again in 2018, to 4.4 percent, its lowest point since 1994.

Although there have been brief periods when residential construction was similarly constrained, the duration of today’s tight conditions is unprecedented. Since 1974, annual additions to the housing supply exceeded household growth by an average of 30 percent to accommodate replacement of older housing, additional demand for second homes, population shifts across markets, and some slack for normal vacancies. According to Joint Center for Housing Studies estimates, annual construction should now be on the order of 1.5 million units, or about 260,000 higher than in 2018.

Several factors may be contributing to the unusually slow construction recovery. For one, the housing boom in the early 2000s created an excess supply of homes. The vacancy rate for housing units for

With the economy on sound footing and incomes ticking up, household growth has finally returned to a more normal pace. Housing production, however, has not. The shortfall in new homes is keeping the pressure on house prices and rents, eroding affordability—particularly for modest-income households in high-cost markets. While demographic trends should support a vibrant housing market over the coming decade, realizing this potential depends heavily on whether the market can provide a broader and more affordable range of housing options for tomorrow’s households.
rent or sale began to climb after 2000 from its long-term average of 4.5 percent to a peak of 6.2 percent in 2009, and it took most of the ensuing decade to work off the surplus. With memories of these conditions still fresh, builders and lenders alike are wary of speculative development that would expand the housing supply too rapidly.

Labor shortages are another possible explanation. The residential construction sector has struggled for years to fill job openings, given that its traditional labor pool—younger men without college educations—is shrinking. With the economy near full employment, competition for workers has intensified, limiting the ability of the construction sector to ramp up quickly.

Meanwhile, the housing that is being built is intended primarily for the higher end of the market. The relative lack of smaller, more affordable new homes suggests that the rising costs of labor, land, and materials make it unprofitable to build for the middle market. By restricting the supply of land available for higher-density development, regulatory constraints and not-in-my-backyard (NIMBY) opposition may also add to the challenges of supplying more affordable types of housing.

**HOMEOWNERSHIP ON THE REBOUND**

After falling for 12 consecutive years, the US homeownership rate edged up in both 2017 and 2018, to 64.4 percent. Although last year’s increase was just 0.5 percentage point, this translates into a 1.6 million jump in the number of homeowners, bringing growth since 2016 to 2.8 million. The largest increase was among households in the key age group of 25–39, whose homeownership rate was up by 2.0 percentage points or some 1.1 million owners in 2016–2018.

This rebound in homeownership comes amid worsening affordability. In the wake of the recession, falling home prices and historically low interest rates produced the most affordable homeownership conditions in decades. After adjusting for inflation, the monthly payment on the median-priced home was just $1,176 in 2012—45 percent below the peak in 2006 and 36 percent below the level in 1990.

Since then, interest rates have remained low but home prices have climbed steadily. Indeed, real prices were back within 2 percent of their 2006 peak at the end of 2018, according to the FHFA Home Price Index. As a result, the monthly payment on a median-priced home stood at $1,775 last year, just 3 percent below its 1990 level and within 17 percent of its 2006 high. Strong income gains among younger households helped to counter the increase, however, with median incomes of households aged 25–34 and 35–44 both growing more than 11 percent in real terms between 2013 and 2017.

The ratio of median home price to median household income is a common yardstick for measuring affordability, indicating how difficult it is for would-be buyers to qualify for a mortgage and save for a downpayment. Nationwide, this ratio rose sharply from a low of 3.3 in 2011 to 4.1 in 2018, just shy of the 4.7 peak in 2005. But conditions for would-be buyers vary widely across the country, with home values more than 5.0 times incomes in roughly one in seven metro areas (located primarily on the West Coast) compared with less than 3.0 times income in about one in three metros (located primarily in the Midwest and South) (Figure 2). In the 100 largest metros with price-to-income ratios above 5.0, the median-income household could afford just 36 percent of recently sold homes on average in 2017. In metros where the ratio is under 3.0, however, the median-income household could afford 84 percent of recently sold homes.
The ability to purchase a home depends largely on access to mortgage financing. Both the Urban Institute and Mortgage Bankers Association indexes show that credit conditions tightened significantly after the crash, particularly for loans to borrowers with less than stellar credit histories. By this measure, conditions in the last few years have remained tight. But there has also been a significant increase in loans with debt-to-income (DTI) ratios above 43 percent. According to a recent Urban Institute report, the share of Fannie Mae loans with such high DTI ratios more than doubled from 13 percent in 2013 to 29 percent in 2018, while the share of Freddie Mac loans was up from 14 percent to 25 percent.

A 43 percent DTI ratio is the cutoff set by the Consumer Financial Protection Bureau for qualified mortgages—loans that borrowers are more likely to be able to afford. This limit does not, however, apply to loans insured by the Federal Housing Administration (FHA) and, at least for the time being, to loans insured by Fannie Mae and Freddie Mac under a temporary exemption. Given the significant growth in mortgage loans exceeding the 43 percent limit, expiration of the exemption in 2021 could result in a substantial shift in lending volumes from Fannie Mae and Freddie Mac to FHA at a higher cost for borrowers or a sharp reduction in credit access for those with these high debt-to-income ratios.

In the years ahead, demographic trends should support growing demand for homeownership as more members of the large millennial generation age into their 30s when homebuying peaks. According to the latest Joint Center projections, if age-specific homeownership rates remained at the same level as in 2018, household growth alone would add roughly 8.0 million homeowners between 2018 and 2028. And if, consistent with recent trends, the overall homeownership rate rises by 1.6 percentage points from the 2018 level, growth in the number of homeowners could reach 10.1 million for the decade.

At the same time, a rise in interest rates and home prices plus a tightening of credit, on top of the limited supply of entry-level housing, could put homeownership out of reach for many more households. The sensitivity of the market to changes in homebuying conditions was evident at the end of 2018 when a jump in interest rates was followed by a slowdown in home sales. Although a retreat in interest rates in early 2019 helped to stabilize the market, the near-term outlook for homeownership still depends on how trends in house prices, interest rates, household incomes, and credit availability affect affordability for first-time buyers.

### RENTAL MARKETS STEADY AMID SLACKENING DEMAND

According to the Housing Vacancy Survey, the number of renter households fell again in 2018. Although down by just 239,000 over two years, even this modest dip is in stark contrast to average annual increases of nearly 850,000 renter households in the preceding 12 years. The declines were widespread, with 31 states losing renters from 2015 to 2017. However, estimates show an uptick in early 2019, in keeping with Joint Center projections of about 400,000 net new renter households annually over the coming decade.
Trends in rents and vacancy rates indicate that rental markets are still on solid footing. The Consumer Price Index indicates that overall rents rose at a 3.6 percent annual rate in early 2019, or twice the pace of overall inflation. Meanwhile, rents for professionally managed apartments were up more than 3.0 percent in more than half of the 150 metros that RealPage tracks, with growth exceeding 5.0 percent in 25 of those markets. Low and falling vacancy rates are keeping the pressure on rents, with the national vacancy rate sliding from 7.2 percent in 2017 to 7.0 percent in the first quarter of 2019. Tightening occurred in all regions of the country and in about two-thirds of RealPage metros.

These conditions seem somewhat at odds with the falloff in demand and the continued strength of rental construction. Indeed, rental completions were near a 30-year high at 360,000 units last year, while starts rose 5.0 percent to 392,000 units. But even as overall demand cooled, higher-income households kept up demand for new apartments. Indeed, even after adjusting for inflation, the number of renters earning at least $75,000 increased for eight consecutive years, rising by 311,000 households in 2017–2018 alone and by some 4.6 million households since 2010.

Changes in the rental stock have also offset some new construction, keeping absorptions in line with supply. Of the 338,000 unit decline in rentals in 2017, most were single-family homes and apartments in two- to four-unit buildings that likely converted to owner occupancy. Thus, even if homeownership rates continue to increase, low vacancy rates and shifts in the existing stock are likely to prevent a significant softening of rental markets.

In fact, weaker overall rental demand could help to ease conditions at the low end. With most new construction targeting the high end of the market, there has been some potential for excess supply to filter down to lower rent levels. But with rental demand far outpacing additions to supply through 2016, this has not happened. In fact, CoStar reports that the vacancy rate for lower-quality rentals was only 4.8 percent at the beginning of 2019, down from 6.7 percent at the end of 2011.

This tightness reflects a substantial drop in the supply of low-cost units as overall market rents climbed. The number of units renting for under $800 fell by 1.0 million in 2017 alone, bringing the total drop in 2011–2017 to 4.0 million (Figure 3). Half of all metros posted declines of more than 10 percent over this period. The falloff was largely concentrated in the West, where the majority of metros lost over 20 percent of their low-rent units. But with rental demand now easing and new supply holding steady, more downward filtering of units could help to slow the shrinkage of the nation’s low-cost stock.

**COST BURDENS IMPROVING OVERALL, BUT RENTERS STILL PINCHED**

The share of US households paying more than 30 percent of their incomes for housing, the standard definition of cost burdens, declined for the seventh straight year in 2017. The latest American Community Survey reports that the share of cost-burdened households inched down 0.5 percentage point to 31.5 percent—some 5.7 percentage points below the 2010 peak. The total number of cost-burdened households in the US also fell by 4.9 million in 2010–2017, to 37.8 million.

Much of this progress was among homeowners, whose overall cost burden rate declined by nearly 8.0 percentage points in 2010–2017, to 22.5 percent—its lowest level this century. At the same time, however, 47.4 percent of renter households remained cost burdened, with the share improving just 0.1 percentage point in 2016–2017 and 3.4 percentage points from the peak in 2011. As a result, cost-burdened renters now outnumber cost-burdened homeowners by more than 3.0 million. In addition, renters make up 10.8 million of the 18.2 million severely burdened households that pay more than half their incomes for housing.

Public concern about a rental affordability crisis has increased in many areas of the country as cost burdens have moved up the income scale. Households with incomes under $15,000 continue to have the highest burden rates, with 83 percent paying more than 30 percent of income for housing, including 72 percent paying more than 50 percent. These shares were largely unchanged between 2011 and 2017, while cost-burden rates climbed 4.6 percentage points among households earning $30,000–44,999 and nearly 2.9 points among those earning $45,000–74,999 (Figure 4).

The spread of renter cost burdens is most evident in expensive metros such as Los Angeles, New York, San Francisco, and Seattle. In the nation’s 25 highest-rent markets, some 46 percent of renter households with incomes of $45,000–74,999 were cost burdened in 2017,
compared with only 30 percent of same-income households across all 100 largest metros. Severe cost burdens are also more common in the 25 highest-rent markets, affecting 28 percent of renters with incomes of $30,000–44,999 and 7 percent of those with incomes of $45,000–74,999. The comparable shares across all 100 largest metros are substantially lower at 16 percent and 4 percent, respectively.

**HOMELESSNESS ON THE RISE IN HIGH-COST STATES**

There have been notable reductions in homelessness over the past decade. According to HUD’s annual point-in-time counts, the number of people experiencing homelessness fell by 87,000 from 2008 to 2018 and by some 38,000 in the last five of those years. This progress reflects an expansion of permanent supportive housing and the widespread adoption of the “housing first” model that provides housing without preconditions for changes in behavior. The improvements have been most evident among populations that have received targeted efforts and resources—veterans, families, and the chronically homeless.

Despite this progress, however, the unsheltered population is on the increase—particularly in certain high-cost Western states. The problem is most acute in California, where the number of unsheltered homeless grew by 25 percent in 2014–2018, to 89,500. Other states with sharp increases in their unsheltered homeless populations are Washington (up 80 percent over this period, to 10,600), Colorado (up more than 100 percent, to 4,300), and Oregon (up nearly 50 percent, to 8,900).

With thousands more individuals living on the streets, the highly visible problem of homelessness has prompted significant commitments of state and local funds for new housing options. In California, voters passed a statewide proposition to provide $2 billion in funding for homelessness prevention initiatives for individuals with mental health issues. In addition, San Francisco raised taxes on the city’s largest businesses to fund housing and social services for the homeless, and Berkeley voters approved a $135 million municipal bond to fund housing for both middle-income households and for those most at risk of homelessness.

Although these measures provide much-needed funds to get people off the streets and into stable housing, a near-record number of renters in these high-cost areas still face significant housing challenges. Meeting the need for decent, affordable housing in these markets will require a targeted and sustained strategy supported by both the public and private sectors.

**THE OUTLOOK**

Although subject to short-term ups and downs in the economy, housing markets are largely shaped by longer-term demographic trends. Over the next decade, two generations will dominate population growth—the millennials (born 1985–2004), with members now clustered around age 28, and the baby boomers (born 1946–1964), with a leading edge now age 73 but with a large share still in their late 50s (Figure 5).
These two large generations will propel growth in 35–44 year-olds and lift the number of older adults to new heights. The Joint Center projects that the number of households in their mid-30s to mid-40s will increase by 2.9 million over the decade, while those age 65 and over should grow by an astounding 11.1 million. Meanwhile, the number of 45–64 year-old households will fall by 1.9 million as the smaller gen-X generation (born 1965–1984) replaces the baby boomers in this age range.

Under these assumptions, the aging baby boomers will add some 8.4 million households that are either single persons or married couples without children living at home. While this surge in one- and two-person households might imply strong demand for smaller homes, most older adults plan to remain in their current homes as they age. To do so, though, many of these households will need to modify their homes to accommodate the physical limitations of aging, fueling strong growth in the remodeling market. But even if a minority of this large age group does choose to relocate, demand for smaller, more accessible homes should also increase significantly.

Within the 35–44 year-old age group, nearly two-thirds of the growth in households over the next 10 years will be among families with children. Given high homeownership rates at this stage of life, demand for owner-occupied housing is projected to grow substantially over the decade. Since many of these households will be first-time buyers, demand for entry-level homes should be especially strong. But today’s relatively low homeownership rates for this age group also imply continuing demand for rental housing, with overall growth in renters projected to average 400,000 per year in 2018–2028.

Whether these projections come to pass depends on a number of factors. Certainly, economic conditions will play a role, since the ability to form independent households is strongly associated with income. The pace of foreign immigration is also critical. As natural increase (births over deaths) in the native-born population declines over the decade, current projections call for the foreign-born population to drive an ever-larger share of household growth. If efforts to curtail immigration prevail, however, future housing demand will be much lower than projected.

Another big question is whether the market can supply housing that is within the financial reach of most households. If housing costs continue to rise faster than incomes, growth of households—and of housing demand—is likely to slow. As it is, the market has only produced enough homes to match the pace of household growth, let alone cover replacement and second-home demand and allow normal levels of vacancies.

If current housing supply trends persist, house prices and rents will continue to rise at a healthy clip, further limiting the housing options for many. To ensure that the market can produce homes that meet the diverse needs of the growing US population, the public, private, and nonprofit sectors must address constraints on the development process. And for the millions of families and individuals that struggle to find housing that fits their budgets, much greater public efforts will be necessary to close the gap between what they can afford and the cost of producing decent housing.