Maybe It Really Does Take a Village: Supporting the Creation of High-Quality Unsubsidized Affordable Rental Housing in Legacy Cities

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Renewing the Promise of the Middle Class

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Context for Naturally Occurring Affordable Housing (NOAH)

• Devolution of public policy from the federal and state governments to “networks of public, private and civic actors...” [Katz and Nowak]

• Subsidy to house the neediest inadequate to meet demand

• Stubbornly high cost burdens for modest-income households

• Production of housing – especially multi-family housing – is skewed towards luxury (Class A) units
  • Some project that housing will “filter down” through the housing market
Towards a Definition of NOAH

- NOAH goes by various names: *unsubsidized affordable housing, market affordable housing*
- Generally created without significant federal subsidy (e.g., LIHTC)
  - Local tax abatements, HCVs, reduced interest rates, etc. don’t disqualify as NOAH
- Tenure mix related to local market characteristics
- Mostly older/rehabbed rather than new construction
• Affordability pegged to 30% of household income
• Targeted incomes generally 60% AMI+ (often above central city average)
• All-in unit cost of $80,000 - $125,000
• Small, family-owned, mission-oriented, “mom-and-pop,” often local or regional ownership
• Rental NOAH stock may include:
  • Single family row homes (Phila., Baltimore, Richmond)
  • >50-year-old multi-family stock often at city edge or in first rings suburbs
  • 2-49 unit B/C (REIS) or 1- and 2-Star (Costar)
What’s Happening in that B/C Multi-family Market?

- Very little B/C unit creation
- Prices rising / vacancies low
- Capitalization ratios in the 6%-8% range
- Cost burdens average 16.5% of income
- Reasonable gross revenue to investors, but less than for A stock
Change in Typical Rent in A vs. B/C Grade Multi-Family Units

Selected Regions

Monthly Asking Rent by Class of Unit in Selected Regions; 2015-2018

<table>
<thead>
<tr>
<th>Class of Unit / City</th>
<th>2015 Asking Rent</th>
<th>2018 Asking Rent</th>
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</thead>
<tbody>
<tr>
<td>A Baltimore</td>
<td>8.7%</td>
<td></td>
</tr>
<tr>
<td>B/C Baltimore</td>
<td></td>
<td>17.1%</td>
</tr>
<tr>
<td>A Philadelphia</td>
<td></td>
<td>14.6%</td>
</tr>
<tr>
<td>B/C Philadelphia</td>
<td></td>
<td>12.8%</td>
</tr>
<tr>
<td>A Pittsburgh</td>
<td>6.7%</td>
<td></td>
</tr>
<tr>
<td>B/C Pittsburgh</td>
<td>12.4%</td>
<td></td>
</tr>
<tr>
<td>A Richmond</td>
<td>8.0%</td>
<td></td>
</tr>
<tr>
<td>B/C Richmond</td>
<td>11.4%</td>
<td></td>
</tr>
</tbody>
</table>

2015 Asking Rent 2018 Asking Rent
Challenges of NOAH Production

- Shortage of NOAH stock and stiff competition – including from Class A developers
- High costs of construction and real estate taxes
- Appraisal gap, especially in more stressed markets
- Risky nature of inexperienced entrepreneurs
  - Poor credit
  - Small portfolio concentrates financial risk
- Financing Challenges
  - Banks are slow, may have minimum loan amounts
  - “Hard money lenders” are expensive, CDFIs have rigorous underwriting/mission criteria
Opportunities of NOAH Housing Production

Practitioners say middle or lightly stressed local submarkets—where property and neighborhood conditions are not seriously impaired—are most appropriate for NOAH.

Can mission-oriented capital use market data to secure concessions on depth/duration of affordability as a trade-off for more favorable transaction terms?
Can Market Conditions Guide NOAH Transactions?

Illustration of MVA and DRR Typology

MVA Typology: Measure of Current Market Conditions

- Strong
- Middle
- Weak

DRR Typology: Measure of Displacement Pressure

- High Pressure
- Steady
- Stabilizing
- Declining
Can Market Conditions Guide NOAH Transactions?

Baltimore. Mixed/Steady Middle Markets with little market pressure: Ideal for SF NOAH / neighborhood preservation strategy.
Can Market Conditions Guide NOAH Transactions?

Richmond. High Pressure Middle & Steady Weak Markets: Rising market pressure in spots ideal for financing tradeoffs; preservation in steady areas.