MTP/SCS

Appendix E-6

Housing Demand White Paper

Changing Demographics and Demand for Housing Types

Sacramento Area Council of Governments

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Note About This Version

This report was originally prepared for and presented to the SACOG Board of Directors in February 2011 updated in November 2011.

Introduction

The U.S. housing market in the coming decades will differ significantly from recent decades with trends toward demand for a changing housing stock. Evolving demographics and preferences held by specific demographic groups, or generational cohorts, are driving the change. On the housing demand side, the aging of the large baby boomer generation, the preferences of the even larger Generation Y cohort (those born between 1978 and 1994), as well as continued immigration will have a major impact on demand. On the supply side, many researchers suggest the type and location of new housing construction over the past few decades may not match anticipated future demand . This poses both constraints and opportunities for future development, redevelopment and reuse. This paper explores national trends. As SACOG continues to develop the Updated MTP2035, the Sustainable Communities Strategy and the Regional Housing Needs Allocation, it will look at statewide and regional trends.

Housing Choices of Generational Cohorts and Immigrants

Baby boomers and Generation Y will drive much of the change

While several demographic factors are evolving, the change in the distribution of age cohorts is probably the most profound factor. Waves of Americans in different age categories each having their own identity, lifestyles and preferences for housing types will impact how the U.S. grows.

A lot of attention has been paid to the baby boomer generation, those born between 1946 and 1964. This large group of Americans currently totals 76 million, and as they age, their changing housing demands and choices create changes in housing markets.

Following them is Generation X, often referred to as the baby bust generation, because of the significant drop-off in births. This generation, born between 1965 and 1977, currently total 45 million people. As this generation goes through life's stages, its smaller size may bring a drop-off in housing demand.

The next wave of Americans is called Generation Y, or Echo Boomers, for primarily being the offspring of the baby boomers. This generation, born between 1978 and 1994, is currently the largest cohort currently numbering 77.4 million, will have a profound impact on the U.S. housing market for decades ahead.

In addition to aging baby boomers and the emergence of Generation Y, a third group will also have a large impact on housing demand: immigrants. National immigration policy, however, will ultimately determine the growth of this group.

Each of these groups and their impacts, particularly due to housing choices now and into the future are examined below.

<u>Baby boomers housing trends and choices</u>

In 2011, the oldest baby boomers turn 65 and a huge wave of retirees is expected over the next two decades. Boomers will become a senior population unprecedented in size. According to the U.S. Census Bureau, 10.4 million boomers are between 55 and 64, a 43 percent increase over the past decade (compared to overall population growth of 9.4 percent).

Baby boomers have always made their presence felt. Immediately after World War II, a huge increase in the national birth rate resulted in enormous demand for consumer goods. As boomers became adults, their needs for housing, cars, college educations and other needs continued to grow. By middle age, as they were raising children, they increasingly demanded single-family housing and roadway expansions to get them to their jobs.

As boomers start to retire, many are seeking more of a senior-friendly lifestyle and housing. Although many are expected to stay in their existing homes and communities, others will choose to downsize homes and/or seek more service-rich environments. Because this generation is so large, the impact on the built environment will be equally large. According to national real estate research firm Roberts Charles Lesser & Company (RCLCO), three-quarters of retiring boomers want to live in mixed-age amenity-rich communities with walkability and access to public transit.

Baby boomers are not all purchasing homes when they move. According to the Harvard University Joint Center for Housing Studies, about two-thirds of renter growth in the past decade was among households aged 45-64, and renter households over age 55 are projected to increase by more than 3 million in the coming decade.

Generation Y housing trends and choices

Generation Y, those Americans born between 1977 and 1994 are currently aged 16-33. The 2007-2009 recession has disproportionately affected this generation with high jobless rates that have evidently impacted their current housing choices. Young adults have increasingly doubled-up with roommates as well as living with their parents. In 2009, 20.3 million 18 to 34 year olds (26 percent) were living with their parents— the highest level in the past 25 years, according to the Census Bureau.

Once the economy settles down, and job growth emerges, housing industry analysts believe young adults who had doubled up will start to form their own households. According to Marcus and Millichap, an international real estate research firm, this is evident in the trend that studios and one-bedrooms have begun to lead the recovery. This highly diverse generation is expected to provide demand for apartments and small housing units a boost over the next 15 years.

In 2008, college enrollment jumped by an unusually large 850,000. The downside to the benefits of more education is that young people will carry more debt. Approximately 66 percent of bachelor-degree recipients held an average of $23,300 in student debts by 2007-08—both record figures. This debt load may limit prospective homebuyers across all ages, including potential new ones from Generation Y, to take on a mortgage.

According to an article in USA Today, in two-thirds of the largest 51 U.S. cities, the urban centers grew twice as fast with college graduates in their 20s and 30s than in the rest of the metropolitan area. In addition, young adults with college educations were 94 percent more likely to live in close-in urban neighborhoods than their less educated counterparts.

The effect of immigration

New immigrants tend to enter the U.S. as young adults, and as such they will increase the Generation Y cohort even more, yet they may have distinctly different characteristics than the traditional Generation Y member. As mentioned earlier, U.S. immigration policy will be the major driver of the future size of this group. The Census Bureau projects annual average immigration between 1.3 to 2.1 million from now through 2050. Even if all immigration were halted, past inflows and higher fertility rates ensure that immigrant households will increasingly drive growth in housing demand. Immigrant households have continued to grow at a faster pace than native-born households.

While immigrants have historically had a higher likelihood of living in attached housing products and in urban areas, this trend has been changing. As city centers seem to be more desirable for baby boomers and those in Generation Y, and the urban cores have gentrified and pushed housing prices up, immigrants are increasingly moving to first-ring suburbs. As immigrants move further toward outer ring suburbs, higher percentages of them than in the past are increasingly looking for larger units with three or more bedrooms and child-friendly configurations. Immigrants are a diverse group and as such will seek a variety of housing product types and sizes in both urban and non-urban areas.

The portion of renter households by foreign-born persons increased from 17.4 percent in 2000 to 19.6 percent in 2009. However, the Joint Center for Housing Studies' State of the Nation's Housing 2010 report states that the immigrant share of first-time home buyers was 19 percent and 12 percent of repeat homebuyers.

Factors in Household Formation

Changes in the rental market

The traditional prime renter age in the U.S. is between 20 and 34, the Generation Y age group. By 2015, the U.S. will have substantially more 20 to 34 year olds than 35 to 49 year olds, according to the Joint Center for Housing Studies. At the same time, the number of households headed by persons under 35—the prime rental group—will grow faster than the overall population.

Looking further out, the Census Bureau predicts that the total U.S. population will increase by 100 million over the next 30 years or more than 3 million annually. This will boost overall demand for various real estate uses, including helping to absorb excess housing inventory and propel greater demand for apartments. Due to the demographic shifts described above, and the corresponding shifts in housing preferences due to the aging of the baby boomers and the entry of Generation Y into the housing market, some market analysts may conclude that there will be a greater demand for compact housing than in the past.

Chris Nelson of the University of Utah writes that the U.S. contains 39 million rental units now, and that number will grow by another nine to 12 million units. Rental units comprised 31 percent of all housing units in 2005; by 2020, that share will increase to 41 percent. One development association, the Urban Land Institute (ULI), argues that these demographic factors will lead to a more frugal population that will adapt to smaller, more efficient living units in areas more convenient to work, shopping, recreation and entertainment. According to ULI's Emerging Trends 2011 report, apartments are one of the only reliable cash-flowing real estate asset categories suitable for core institutional investors, such as insurance and pension funds. ULI contends that the demographic trends that will shape the new decade arrived in 2010. That year, absorption rates for apartments were the strongest in a decade, with 77,000 units absorbed in the first half of 2010, despite U.S. unemployment hovering around 9.5 percent; had unemployment been lower, the absorption rate for apartments would have likely been higher.

Changing rates of marriage

Americans, especially those in Generation Y, are taking longer to settle down, if they settle down at all. The median age of first marriage is increasing. In 1970, the median age for a man was 23 and 21 for a woman; today those are 28 and 26, respectively. According to the Council on Contemporary Families, a Chicago-based research firm, for the first time in more than a century, more than half of those aged 25 to 34 have never been married. Prolonged "emerging adulthood" means putting off getting married, and likely increasing the potential pool of renters.

Changes in household size and composition

There is a persistent perception that the typical household is a married couple with children, but that has not been true for some time. Less than a quarter of U.S. households in 2006 fit that description. Instead, according to the Joint Center for Housing Studies, the fastest growing segment is the single-person household, and going forward, the Center for Housing Studies states that couples without children will grow at an even faster rate.

University of Southern California Professor Dowell Myers notes that the rapid rise in one-person households will likely continue for the next several decades. He cites a study by Zeng, et al, that 25.7 percent of all U.S. households were one-person households in 2000. Projections for 2030 indicate that single person households may grow to 33.8 percent, and up to 37.3 percent by 2050. In today's terms, each one percent represents 1.3 million U.S. households.

Multi-generational household growth

According to the Pew Research Center, in 1980, 28 million Americans (12 percent) lived in a family with at least two adult generations (i.e., a grandparent and at least one other generation). In 2008, that figure was estimated at 49 million Americans, or 16 percent of the U.S. population. This trend affected adults of all ages. Today, one-in-five adults ages 25 to 34 lives in a multi-generational household, as do one-in-five adults age 65 and older.

The growth in multi-generational households is the result of demographic and cultural shifts, including the rising share of immigrants in the population and the rising median age of first marriage in all adults. In addition, the Pew report found that, from 2007 to 2008, during the height of the recession, the number of Americans living in a multi-generational family household grew by 2.6 million.

Prediction for New Housing Growth

Over half of development in 2025 may not have existed in 2000

According to research conducted by Arthur Nelson, Director of the Metropolitan Research Center at the University of Utah, over half of all development on the ground in the U.S. in 2025 will not have existed in 2000. He concludes that by 2025, much of society will have been spatially rearranged, or urban land use patterns will change. He claims that the spatial rearranging will be driven by changes in the type and location of housing that will be demanded by baby boomers and Generation Y. He concludes that the need for new units is equally divided between attached units (i.e., apartments, townhouses and condos) and small-lot houses (i.e., one less than one-sixth of an acre). Nelson further states that there will be no net increase projected in the need for houses on larger lots. His projection highlights that there is currently an imbalance between population preferences for housing type relative to the existing characteristics of existing housing stock.

<u>New housing only serves 1 to 2 percent of all households</u>

Professor Myers holds that new construction does not respond to average growth in demand. Rather, he argues, that only 1 to 2 percent of all households each year lives in newly constructed units, and it is this small minority that is served by developers of new housing. However, Myers believes that this segment is not representative of the population as a whole and is drawn disproportionately from population groups that are growing faster than the supply that they prefer. He concludes by stating that demographic change has the potential to drive major shifts in development patterns if the growing demographic categories in one generation (e.g., Generation Y) have very different preferences in product types than those of a prior generation, (e.g., baby boomers).

<u>Household without children</u>

The New Urban Network reported that University of Utah Professor Chris Nelson identified that 90 percent of the increase in the demand for new housing will come from households without children, and 47 percent of that will be from senior citizens, many of whom are. The “great senior sell off” as Nelson describes it, is when those 65 or older move. As they move, 80 percent who sell their homes will vacate single family houses, but only 41 percent will move back into single family houses. The rest will move into multi-family buildings.

<u>Housing preferences of Generation Y may not match available stock</u>

In another article, Myers and SungHo Ryu argue that the future population and age structure will lead to differences between age and home buying and selling. The aging, retirement and lifestyle patterns of the 76 million baby boomers will likely shape U.S. housing markets and trends for decades ahead. They conclude that there will be an oversupply of homes offered for sale by aging baby boomers – many of which may not be of the housing type that young buyers want. The researchers raise the idea that where decline once occurred as housing moved from the central city to the suburbs, it may now be reversed as the suburbs will see surpluses of large-lot single-family housing.

Other Conditions that Could Impact the U.S. Housing Market

Homeownership may decline

The U.S. homeownership rate dropped to 66.9 percent (down 2.3 percent) since 2004, and continues to drop according to *Time* magazine. Prudential Real Estate Investors project that by 2015 the homeownership rate will drop to 64 percent.

Energy costs

Climate change, fuel prices, and policies on climate change and energy all could have an impact on housing types. Future higher energy costs could act to reduce the preferred housing unit size and encourage more central locations that reduce the cost of transportation.

Lingering effects of the housing bubble

The sub-prime mortgage crisis and the end of the housing bubble may have long-term repercussions for housing finance and affordability. The relative shortage of new demand (created by the vacuum of Generation X) to offset the increasing quantity of households leaving the housing market (created by seniors trying to sell their homes) could lead to an oversupply of large lot homes for sale.

Tightening credit standards affects homeownership

The impacts of the housing bubble also include the increased standards for mortgage lending, as mentioned earlier. With lenders requiring larger down payments and higher credit scores, many prospective homebuyers may no longer qualify to purchase homes, and hence the reason for the decline in the percentage of homeownership since 2004 cited earlier.

Lower median household incomes than a decade ago

Median household incomes for all age groups in each income category are likely to have ended the decade lower than where they began in 2000. According to Harvard University’s analysis of Census Current Population Survey (CPS) data as last measured in March 2009, no group was spared from income declines. If incomes do not rebound quickly, Americans will have to consider whether to cut back on the size and features of their homes or allocate larger shares of their incomes to housing.

Next Steps

SACOG will continue to examine demographic trends at the national, state, and local levels, and collect data about the six-county Sacramento region to better understand where the housing market may lead in the future. The Appendix of this document shows some preliminary data as it relates to the SACOG region.

Annotated Bibliography

The following are summaries of the literature review that was cited in the Housing Demographics White Paper.

[01] Area 4 Agency on Aging. January 2009. “The Dual Challenge: Sacramento County.”Email, August 3, 2010. This documentation provides information about seniors in Sacramento County. This information states that every day 45 residents in Sacramento County turn 60. The fastest growing demographic is centenarians (people over 100). By 2030, Sacramento County will have more people over 60 than children under 18.

[02] Ascierto, Jerry. November/December 2010. “Market Movers: How the emergence of Generation Y, the aging of baby boomers, and immigration trends will impact the multi-family industry in the next decade,” pp. 17-22. *Apartment Finance Today*, This paper discusses the emergence of Generation Y, the aging of baby boomers, and how immigration trends will impact the multifamily industry in the next decade. This is the main paper that addresses the White Paper – The Changing Demographic Trends and the Projected Increase in Demand for Rental Housing. Less than one-quarter of U.S. households have two parents and children in them. The fastest growing segment is single-person households and going forward, married couples without children.

[03] Center for Continuing Study of the California Economy. February 18, 2010.“The SACOG Region: A Decade of Slow Growth: What will the Future Bring?” Presentation. This Powerpoint by Stephen Levy addresses growth rates over the next decade for the SACOG region.

[04] Doherty, Patrick C and Leinberger, Christopher B. November/December 2010. “The Next Real Estate Boom.” *Washington Monthly*. This article elaborates on the changing demographics and their impact on the housing market – more highly compact urban products will be in very high demand while low density suburban projects have an excessive oversupply that will grow as more baby boomers retire.

[05] El Nasser, Haya. April 1, 2011. “Young and Educated Show Preference for Urban Living.” *USA Today*. This newspaper article states that educated people in their 20s and 30s are flocking to live in downtowns across the country, even in urban areas that are losing population. In two-thirds of the largest 51 cities, college educated population in the past decade grew twice as fast within three miles of the urban center as in the rest of the metropolitan area – up an average of 26 percent compared with 13 percent in other parts. The article cites that in 2000, young adults with college degrees were about 61 percent more likely to live in close-in urban neighborhoods than their less educated counterparts. Today, they are 94 percent more likely.

[06] Epstein, Gene. July 26, 2010. “Renter Nation.”*Barrons*. This article addresses why the recession and shifting demographics will swell the ranks of people who will rent, not buy, housing over the next five years.

[07] Ford, Jane. February 9, 2011. "Changing Demographics Play a Key Role in Housing Crisis." *USA Today*. This article from cites that changing demographics are the main cause of today's housing surplus, according the William Lucy, University of Virginia Professor of Urban Planning. Excess supply is linked to the increase of homeowners over age 55 who want to sell and downsize, coupled with the decrease in 30 to 45 year olds who want to buy. From 2000-2009, the number of age 55+ increased by 8 million, while the number of potential 30 to 45 year olds decreased by 3.6 million. The ratio of baby boomers to young adults was five-to-one in 2010, a dramatic increase from 3.5-to-1 in 2000 and 3-to-1 in 1990.

[08] Harvard University Joint Center for Housing Studies., 2011, "The State of the Nation's Housing 2010." This paper summarizes a major study on the status of the nation's housing and which direction it is heading. It projects that household growth will average about 1.48 million annually from 2010 to2020. The high end growth estimate would support production exceeding 1.9 million units per year on average over that decade. Nationally, minorities have accounted for 35 percent of first time homebuyers during the housing bust. The impact on immigration, even if dampened from national immigration policies, will give demand for apartments and smaller starter homes a lift over the next 15 years.

[09] Kalita, Mitra and Robbie Whelan. January 14, 2011. "No McMansions for Millenials." *The Wall Street Journal*. This article reports that a study by the National Association of Home Builders that 88 percent of Generation Y respondents want to live in an urban environment and one-third are willing to pay more to walk everywhere.

[10] Kasler, Dale. October 15, 2010. "Capital region's new home sales sink to new low." *The Sacramento Bee*. This article discusses the new low in new home sales for the third quarter of 2010 in the Sacramento region. Only 1,389 new homes sold for the first three quarters of the year compared to 17,155 in 2004.

[11] Kiviat, Barbara. September 6, 2010. "Rethinking Homeownership", *Time* Magazine, This cover article discusses how homeownership has changed with the current recession. The clear trend is that homeownership rates across the county will be going down.

[12] Lachman, Leanne M, and Deborah L. Brett. January/February 2011. "Generation Y: America's New Housing Wave." *Urban Land*. This article summarizes the results from a survey conducted by ULI on Generation Y regarding homeownership and where they wish to live.

[13] Leong, Pamela J., U.S. Department of Housing & Urban Development Economist, San Francisco. October 25, 2010. Email, This summarizes some of the HUD economist's findings: Homeownership rate in Sacramento is 62.5 percent and California's is 56.3 percent.

[14] Myers, Dowell. May 21, 2007. "Imperatives of Demographic Change."Presentation to Demographic Workshop. This powerpoint presentation focuses on demographic changes (particularly immigration and aging) in the Los Angeles area and their impacts on housing. It concludes that there will be a huge baby boomer sell-off and a new demand for dense environments with reductions in energy consumption.

[15] Myers, Dowell and SungHo Ryu. Winter 2008. "Aging Baby Boomers and the Generational Housing Bubble." *Journal of the American Planning Association* This article continues the analysis in the John Pitkin article and the Chris Nelson research by proposing a method for estimating average annual age-specific buying and selling rates. It also analyses the likely supplier responses to diminished demand.

[16] Nelson, A.C. 2006. "Leadership in a New Era." *Journal of the American Planning Association*, 72 (4), pp. 393-405. This abstract summarizes the comments made in the John Pitkin article above. These changes will drive the rebuilding of much of America's built environment.

[17] Pitkin, John, and Dowell Myers. 2008. "U.S. Housing Trends – Generational Changes and the Outlook to 2050." Transportation Research Board Special Report 298. This paper examines how the baby boomers are aging, retiring, relocating and withdrawing from the housing market will shape housing for decades to come. Nelson is quoted, "over half of all development on the ground in 2025 will not have existed in 2000, even more important is that by 2025 much of society will have been spatially rearranged."

[18] Robert Charles Lesser & Co. Research and Development, (no date). "The Gen Y Cohort." Presentation. This powerpoint was developed for the Seltzer Property in Sacramento. It states that 34 percent of all households will be single person, and childless households will represent 69 percent. Women with Incomes and No Kids (WINKS) represent 43 percent of all Generation Y households and will domination the urban landscape. Eighty-five percent of net household growth between 2010 and 2025 will consist of households without children. The largest year of age 22 Generation Y cohorts took place in 2009, creating the largest rental demand. If this group rents for three years, then it will create the largest demand for first time homebuyers between 2013 and2018 than ever before. Generation Y and Generation X have a strong preference for urban areas and walking to work.

[19] SANDAG. February 26, 2010. "2050 Regional Forecast staff report to SANDAG Board of Directors." This staff report summarizes how SANDAG developed its Regional Housing Needs Allocation (RHNA) projections.

[20] Steuteville, Robert., April 28, 2011 "The Coming Housing Calamity." *New Urban Network*, Part 1. This two-part internet article summarizes Chris Nelson, the University of Utah.Presentation. titled, "The Decade of Calamity" noting that prior to the housing crash the U.S. faced a massive oversupply of large-lot single family houses and an undersupply of multi-family units. The demand for new housing will come from demographic sectors: 90 percent of the increase will be households without children, and 47 percent will be senior citizens, many who are baby boomers. The "great senior sell-off" is when those 65 or older move, 80 percent vacate single family houses, but only 41 percent move into single family units. The rest move into multi-family buildings for a variety of reasons such as low maintenance and proximity to services. Other factors that create the upcoming housing calamity are the declining household size and the decline in homeownership, more stringent rules for mortgages. Nelson concludes

that there will be fewer owner-occupied homes in 2020 than in 2010, despite the rising population during that decade.

[21] Steuteville, Robert, April 29, 2011, "The Coming Housing Calamity." *New Urban Network*, Part II. This article focuses on how public officials can provide the right framework for the upcoming domination of market demand for rental and transit-oriented development. Nelson projects that the rental housing market in the U.S. will grow from 31 percent in 2005 to 41 percent in 2020. The U.S. contains 39 million rental units now, and that number will increase by 9 to 12 million by 2020. This trend is underway, as apartment demand is at is strongest absorption rate in a decade. The presentation includes market studies illustrating the demand for urban living. Seventy percent want to walk to discernable destinations from transit to grocery stores, a trend that had not been seen before. The article also cites three independent studies – the National Association of Realtors, Robert Charles Lessor & Co. (RCLCo) and Nelson – that all found a nearly identical imbalance of U.S. housing supply and demand. The 2009 American Housing Survey found that 28 percent of housing is attached, compared to the three studies that concluded that 38-39 percent of housing demand for this type; likewise, small lot detached comprises 29 percent, whereas demand is for 37 percent; and large lot comprises 43 percent while demand is for 24-25 percent. Nelson's conclusion is that attached and small lot housing is undersupplied by 12 million and 13.5 million units respectively. One of the main obstacles is that public officials need to establish an infrastructure and regulatory framework that promotes walkable, transit-friendly development.

[22] Sullivan, Jenny. March 16, 2010. "High Housing Prices? Don't Blame Land Conservation." *Builder,* 2010. This article summarizes a study by Stanford University that concludes that land conservation does not raise housing prices in nearby areas.

[23] Taylor, Paul et al. March 18, 2010. "The Return of the Multi-Generational Family Household." *Pew Research Center - A Social and Demographic Trends Report*. This paper documents major changes in family household living arrangements that have unfolded over the past three decades and accelerated during the Great Recession. The main trend is that multiple generations of families are living together.

[24] U.S. Department of Housing and Urban Development. July 1, 2010. "Comprehensive Housing Market Analysis: Sacramento, California". This paper discusses HUD's analysis of the Sacramento region broken down into three submarkets. It cites that 73 percent of new condos and infill in Sacramento County are in the city of Sacramento. It also includes statistics on multifamily construction, calling it quite active during the past decade.

[25] Urban Land Institute, October, 2010, "Emerging Trends in Real Estate 2011." This is ULI's end of year forecast for the upcoming year. It identifies apartments with the highest investment prospects among different real estate classes. Other investment classes have much poorer prospects according to the research.