# Rental Affordability Is Worsening

An acute shortfall of affordable rental units makes life more challenging for millions of people nationwide, and it could become even harder for many of them if the trend continues. Although multifamily housing construction is back to historically average levels, the new units flowing into the overall rental supply are generally serving higher-income renters. The combination of increasing rents, stagnant household incomes, and potential changes to public subsidies on the demand-side (Section 8 vouchers and contracts) and the supply-side (public housing and the Low-Income Housing Tax Credit program) has severely constricted the number of available units that are affordable to lower-income renters and that meet their specific needs for location and unit size.[1]

This reality most adversely affects very low-income (VLI) households, defined as those with incomes no greater than 50 percent of area median income (AMI). As rents continue to increase without a corresponding increase in incomes, households with lower incomes cannot afford market rents. This is well documented and the impact is measured in a variety of ways, but it can seem abstract with current metrics. A new Freddie Mac approach provides specific analysis that helps clarify the view into market dynamics and the magnitude of this issue.

### A New Perspective

To make matters plainer, we analyzed loans that Freddie Mac Multifamily financed twice[2] between 2010 and 2016 (the latest period for which data is available). Exhibit 1 shows the total number of underlying units in these repeat financings and compares how and whether they qualified at different levels of affordability between first and second financing.

The results are striking. At the first financing, 11.2 percent of the total number of underlying rental units across the United States were categorized as affordable to very low-income households. At the second financing, rents had increased so significantly that just 4.3 percent of the same units were categorized as affordable to VLI households.

**Exhibit 1: Repeat Financing Very Low-Income Affordability Analysis**

**2010 - 2016**

| | | First Financing | | | | Second Financing | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Units** | **VLI** | **LI** | **Median** | **None** | **VLI** | **LI** | **Median** | **None** |
| **Total** | 97,061 | 11.2% | 71.3% | 13.3% | 4.2% | 4.3% | 65.2% | 21.0% | 9.4% |

Source: Freddie Mac

[1] "America's Rental Housing: Expanding Options for Diverse and Growing Demand," Joint Center for Housing Studies of Harvard University, December 2015, available at http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/ch_2_rental_housing_supply_from_americas_rental_housing_2015_web.pdf.

[2] Such loans include conventional units considered for goals counting purposes utilizing property rent rolls with data available and not any units using estimation methods or LIHTC set aside percentages to determine affordability. The method generally includes 90% of eligible units in each year and excludes, for example, senior housing and student housing.

### Impacts Vary Across the Country

Looking underneath the total at the nine states where Freddie Mac Multifamily financed the most rental units twice during this period, the overall change in affordable VLI units between the first and second financing varies greatly by state, as Exhibit 2 shows. In seven of the states (as highlighted), a significantly smaller percentage of rental units qualified as VLI during the second financing. In Colorado, for example, the number fell from 32.4 percent to just 7.5 percent of the units. In North Carolina, it plunged from 9.8 percent to just 0.3 percent.

As a reminder, we analyzed the affordability of the exact same units at two different, but close, points in time. The results reflect no change in the population of units evaluated. The low VLI hit rates in some states, and drop-off in others, often reflects that households in these areas pay more than 30 percent of their income on rent; the definition of VLI affordable units assumes that housing accounts for no more than 30 percent of income. That assumption is less true as rents increase faster than incomes, and is less true in some metros than in others, something we described this in a previous paper.[3]

**Exhibit 2: Repeat Financing Very Low-Income Affordability Analysis, by State**

**2010 - 2016**

| | | First Financing | | | | Second Financing | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Units** | **VLI** | **LI** | **Median** | **None** | **VLI** | **LI** | **Median** | **None** |
| **U.S.** | 97,061 | 11.2% | 71.3% | 13.3% | 4.2% | 4.3% | 65.2% | 21.0% | 9.4% |
| TX | 28,533 | 10.2% | 74.0% | 13.6% | 2.2% | 3.2% | 69.0% | 23.1% | 4.8% |
| FL | 13,197 | 1.5% | 60.2% | 34.1% | 4.0% | 1.6% | 38.7% | 39.6% | 20.2% |
| GA | 9,766 | 11.8% | 75.9% | 8.7% | 3.6% | 2.1% | 77.7% | 14.8% | 5.4% |
| CO | 5,128 | **32.4%** | 67.6% | 0.0% | 0.0% | **7.5%** | 82.6% | 9.5% | 0.4% |
| NC | 5,061 | **9.8%** | 88.2% | 2.0% | 0.0% | **0.3%** | 83.9% | 15.6% | 0.3% |
| CA | 4,776 | 2.3% | 55.6% | 15.6% | 26.6% | 2.5% | 9.8% | 27.1% | 60.6% |
| AZ | 4,154 | 34.0% | 65.5% | 0.7% | 0.0% | 21.8% | 74.5% | 3.3% | 0.0% |
| NV | 3,564 | 15.8% | 67.6% | 16.4% | 0.3% | 4.0% | 75.4% | 20.1% | 0.5% |
| WA | 3,262 | 4.0% | 86.1% | 1.6% | 8.3% | 1.1% | 81.6% | 11.0% | 6.3% |

Source: Freddie Mac

Although more rental units qualified as VLI between financings in Florida and California, states where housing costs already are high, the increase was minimal (0.1 percent in Florida and 0.2 percent in California) and the percentage of units considered VLI in these two states stayed below 3 percent during both financings.

A more critical finding in California - in addition to the relatively flat trend of available units for VLI households, the number of rental units affordable to even median-income renters (those earning between 80 percent and 100 percent of AMI) fell sharply. During the first financing, 73.4 percent of the rental units funded were affordable to median-income renters. That percentage dropped to 39.4 percent by the second financing. Again, these are the exact same multifamily units evaluated for affordability at two different, but close, points in time.

[3] "Multifamily Affordability: Market Conditions and Policy Perspectives" available at *http://www.freddiemac.com/multifamily/pdf/mrp_affordable.pdf*.

### Broadening the Analysis

To substantiate that our affordability analysis is representative of the broader market, we reviewed all properties[4] that Freddie Mac Multifamily funded from 2010 to 2016 and then trended rents at those properties using vendor (Axiometrics) rent-growth data. The first table in Exhibit 3 shows the number of units funded each year that qualified as VLI, using a population with consistent rules for counting affordability; the second table shows the change in percentage of VLI-affordable units year-over-year. For each year following the initial funding, those same property rents are trended and tested against each respective year's VLI threshold. For example, of the 17,510 underlying units that qualified as affordable to VLI households in 2010, just 3,894 would have qualified in 2016, a drop of 77.8 percent. The drop is steeper in this analysis because all multifamily properties are trended across all years.

**Exhibit 3: Trended Results**

| | Axiometrics Trended VLI Units | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Year Funded | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Total Decline |
| 2010 | 17,510 | 13,851 | 11,101 | 6,412 | 4,985 | 5,032 | 3,894 | -13,616 |
| 2011 | | 27,910 | 23,044 | 13,361 | 9,161 | 9,714 | 7,013 | -20,897 |
| 2012 | | | 43,662 | 27,820 | 20,189 | 21,863 | 16,693 | -26,969 |
| 2013 | | | | 39,833 | 30,982 | 30,265 | 25,953 | -13,880 |
| 2014 | | | | | 34,098 | 33,092 | 25,492 | -8,606 |
| 2015 | | | | | | 66,072 | 51,379 | -14,693 |
| 2016 | | | | | | | 59,530 | |

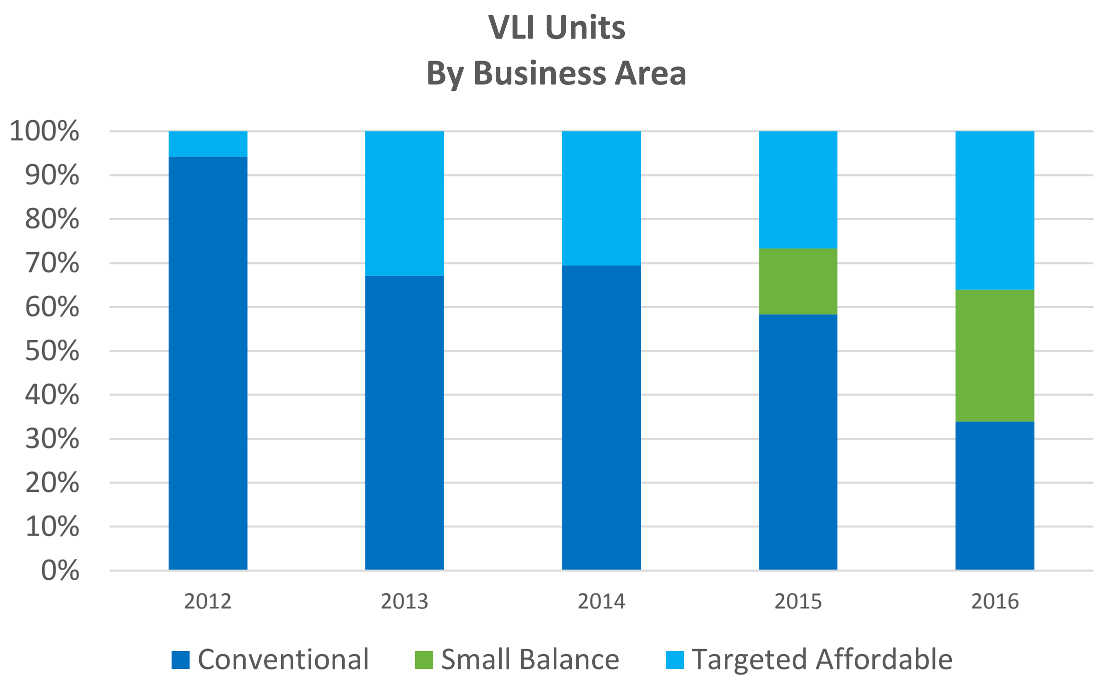
| | % Change in Axiometrics Trended VLI Units | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Year Funded | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Total Decline |
| 2010 | | -20.9% | -19.9% | -42.2% | -22.3% | 0.9% | -22.6% | -77.8% |
| 2011 | | | -17.4% | -42.0% | -31.4% | 6.0% | -27.8% | -74.9% |
| 2012 | | | | -36.3% | -27.4% | 8.3% | -23.6% | -61.8% |
| 2013 | | | | | -22.2% | -2.3% | -14.2% | -34.8% |
| 2014 | | | | | | -3.0% | -23.0% | -25.2% |
| 2015 | | | | | | | -22.2% | -22.2% |
| 2016 | | | | | | | | |

### Innovation Matters

Even in the face of these dramatic market changes, Freddie Mac Multifamily has consistently met its mandated affordable housing goals. We developed products during this period that allowed us to expand our presence in markets that tend to support affordability, as shown in Exhibit 4.

[4] Subject to the same exclusions and filtering methods described in footnote two in the repeat financing analysis described above.

**Exhibit 4: Repeat Financing Very Low-Income Affordability Analysis**




In 2012 our VLI goal was 59,000 units and more than 94 percent of our affordable units came from our conventional business. In 2016 the VLI goal was 60,000 units, but the percentage of our VLI units funded from our conventional business fell to less than 34 percent, or less than 25,000 units. This drop occurred despite our consistent business approach to the conventional market, which we believe has been a representative sample of the overall market in each year of the analysis. In that year, our Targeted Affordable Housing business[5] and our Small Balance Loan program[6] funded 36 percent and 30 percent of the VLI units, respectively.

Significant research on market trends suggests worsening affordability in the rental market. Our property-specific analysis further illustrates the issue. The affordability gap will continue to widen if no action is taken. Even as Freddie Mac Multifamily funds units that are affordable to lower-income renters, those units will not stay affordable for long if rents grow at market-level rates. To make a real, lasting difference, those of us participating in the multifamily rental housing market must make sure that we understand market needs. There are factors that make things difficult and are not easily controlled, such as land and construction costs. But as we source capital to the rental market, we need to look for opportunities to carefully target capital to build and maintain units that are affordable to lower-income households, especially those that have incentives to stay that way.

[5] The Targeted Affordable Housing business focuses on subsidized housing.

[6] The Small Balance Loan program focuses on properties containing five to 50 units and loans ranging from $1 million to $6 million.