



# 4 Homeownership



Despite record-low housing prices and mortgage interest rates, the national homeownership rate continued its slide in 2011. With upwards of two million foreclosures still in process and a rising number of households choosing to rent, further declines lie ahead. Tight credit conditions amid uncertainty in the mortgage market are dampening the recovery in homebuying, while depressed prices are preventing many distressed homeowners from refinancing to more affordable loans.

## HOMEOWNERSHIP TRENDS

The US homeownership rate fell another 0.8 percentage point in 2011, the largest drop in seven consecutive years of decline. At 65.4 percent in the first quarter of 2012, the national rate stood at its lowest level since the first quarter of 1997 and 3.8 percentage points below the peak in the fourth quarter of 2004.

The persistent decline reflects both the high level of foreclosures and the slowdown in households moving into homeownership. Together, these forces have reduced the number of homeowners while increasing the number of renters. The particularly large drop last year represents an acceleration in both trends, with the number of owner households down by 350,000 and the number of net new renters up by 1.0 million (**Figure 18**). Measured from the peak number of homeowners in 2006, there were 1.0 million fewer owners and 3.9 million more renters at the end of 2011.

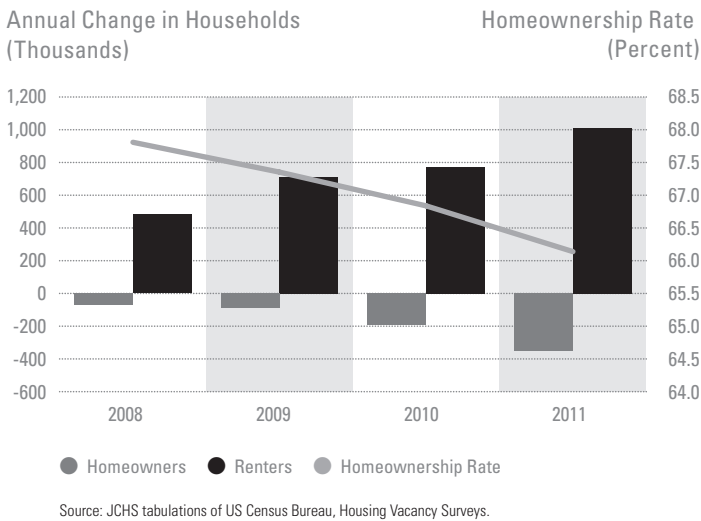
Nevertheless, on net 4.3 million households under age 35 and 730,000 households aged 35–44 joined the ranks of homeowners in 2005–10 (**Figure 19**). This does, however, represent a significant slowdown from 2000–5, when 6.5 million owners under age 35 and 2.6 million aged 35–44 were added on net. Moreover, recent growth in the number of younger homeowners was not enough to offset the typically large losses of homeowners aged 75 and over, thereby bringing down the total number.

But even if younger households pick up the pace of homebuying, working off the backlog of foreclosures is likely to keep homeownership rates on the decline in 2012. The number of loans in the foreclosure process remains high despite an 8.5 percent decline from the 2.1 million peak in 2010. More promisingly, though, the number of loans 90 or more days past due fell almost steadily from 2.3 million at the end of 2009 to 1.3 million in the first quarter of 2012 (**Figure 20**).

Delays in completing foreclosures are longest in states where the courts are involved in the process. The foreclosure inventory in states with judicial procedures stands at 6.5 percent, significantly higher than the 2.5 percent in states with non-judicial procedures. But the robo-signing scandal, ignited by the discovery that loan servicers had not fully and appro-

FIGURE 18

### Losses of Homeowners and Increases in Renters Accelerated in 2011



homeownership for some delinquent borrowers, it offers too little relief to make a meaningful difference in overall foreclosure volumes.

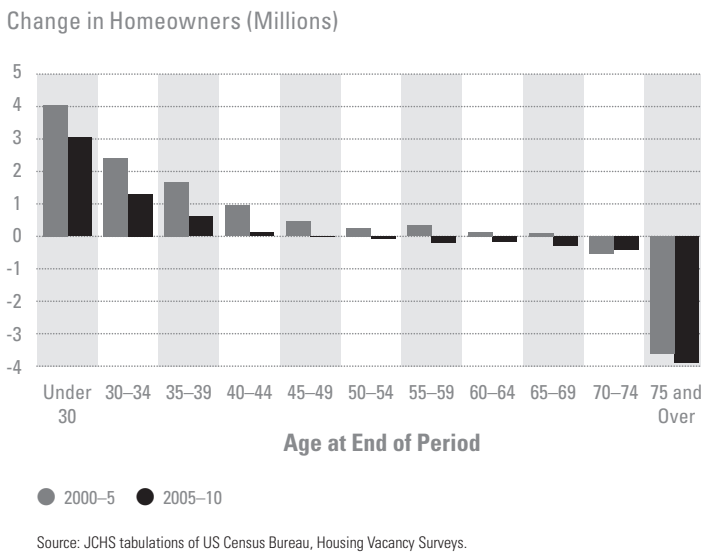
### THE HOMEOWNERSHIP BOOM AND BUST

Homeownership rates have fallen significantly from their mid-2000s peaks across all age groups except seniors. Declines exceed 5.0 percentage points for households up to age 44, 4.5 percentage points for 45–54 year-olds, and 3.2 percentage points for 55–64 year-olds. Indeed, rates for households between ages 35 and 54 have dipped below the trough hit in the early 1990s. At the same time, homeownership rates for households 65 and over have largely held steady at around 81 percent.

Just as the homeownership boom lifted minority rates the most, the homeownership bust brought minority rates down especially hard. After jumping 7.2 percentage points from 1994 to 2004, black homeownership rates dropped back by 4.3 percentage points from 2004 to 2011—nearly twice the decline in white rates (Figure 21). As of 2011, the gap between black and white rates was wider than in 1994. Hispanics held onto more of their 8.5 percentage-point gain during the boom, losing just 2.7 percentage points since the bust. As a result, the white–Hispanic homeownership gap, though still large, was 1.8 percentage points narrower in 2011 than in 1994.

FIGURE 19

### Despite Declining Homeownership Rates, Millions of Young Households Became Homeowners in the Second Half of the 2000s



Households with children have posted the largest losses in homeownership. Since the peak, the rates for married couples with children plunged 5.1 percentage points while those for single-parent and other families with children were down 4.6 percentage points (Figure 22). By comparison, the declines for married couples without children (1.3 percentage points) and other childless families (2.0 percentage points) are more modest. Homeownership rates for non-family households, which include a substantial share of single persons, have also changed relatively little.

Homeownership losses are widespread geographically. From 2006 through 2010, rates fell in all but four less populous and largely rural states (Alaska, Montana, North Dakota, and Wyoming), which all appear to have benefited from booming oil and natural gas production. Understandably, states hard-hit by foreclosures (such as Nevada, Arizona, and California) are among those with the largest declines. But several states that were less affected by the foreclosure crisis (including Minnesota, Colorado, Washington, and Oregon) also had sharply lower homeownership rates thanks to rapidly growing renter populations.

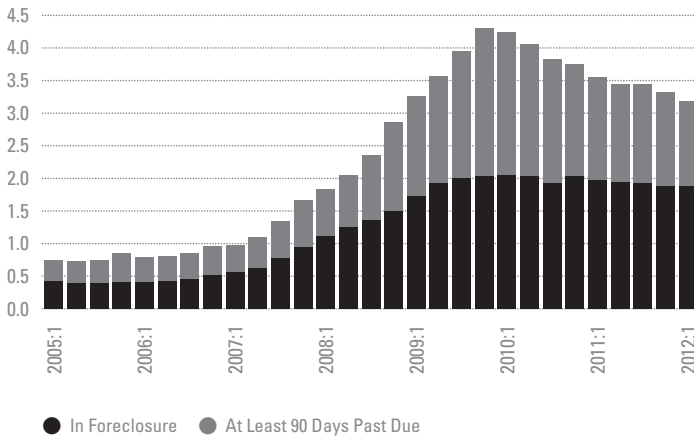
privately documented their legal rights to foreclose, undoubtedly added to backlogs. The February 2012 agreement reached between the nation’s five largest servicers and the government should help to speed up resolutions. The accord also provides funding that states can use for foreclosure prevention initiatives, although many have opted to apply the funds to close general budget gaps. While the agreement should preserve

### SEEDS OF RECOVERY

According to the Freddie Mac Primary Mortgage Market Survey, interest rates on a 30-year fixed mortgage averaged just 4.45 percent in 2011 before sliding below 4.0 percent in early 2012—its lowest level since recordkeeping began in 1971. Together with ongoing house price declines, these historically low rates

FIGURE 20

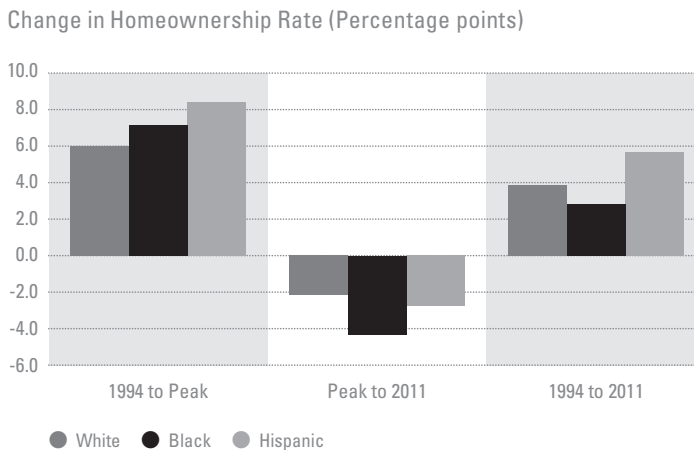
**While the Number of Distressed Loans Is Falling, the Foreclosure Backlog Remains Stubbornly High**  
Number of Loans (Millions)



Note: MBA estimates that the survey covers 85–88 percent of loans outstanding.  
Source: JCHS tabulations of Mortgage Bankers Association, National Delinquency Surveys.

FIGURE 21

**Minority Homeownership Losses Were Disproportionately Large, But Their Current Rates Still Exceed 1994 Levels**  
Change in Homeownership Rate (Percentage points)



Notes: White and black householders are non-Hispanic; Hispanics may be of any race. Homeownership rates of white and black householders peaked in 2004, and Hispanic rates peaked in 2006.  
Source: JCHS tabulations of US Census Bureau, Housing Vacancy Surveys.

have made homebuying a comparative bargain (Table A-6). Indeed, the NAR affordability index hit unprecedented levels in 2011. With renewed weakness in prices spreading to more than half the states, the ratio of the median existing home sales price to median household income edged down from 3.5 in 2010 to 3.2 last year.

Applying the assumptions in the NAR index (a 20-percent downpayment and a 30-year fixed-rate mortgage), the monthly payment for principal and interest on the median-priced home dropped another 6.6 percent in 2011 from a year earlier, to just \$669. As a result, mortgage payments on the median-priced home stood well below the median gross rent for the first time since the early 1970s. For buyers able to put only 10 percent down, the monthly mortgage payment would also be comfortably below the median rent.

Of course, this is not an apples-to-apples comparison in that homeowners not only pay for property taxes, insurance, and maintenance, but they may also experience capital gains or losses from ownership. In addition, the median rental unit is not comparable in size and quality to the median home sold. Still, as renters consider their housing options, homeownership has rarely measured up more favorably.

**BORROWING CONSTRAINTS**

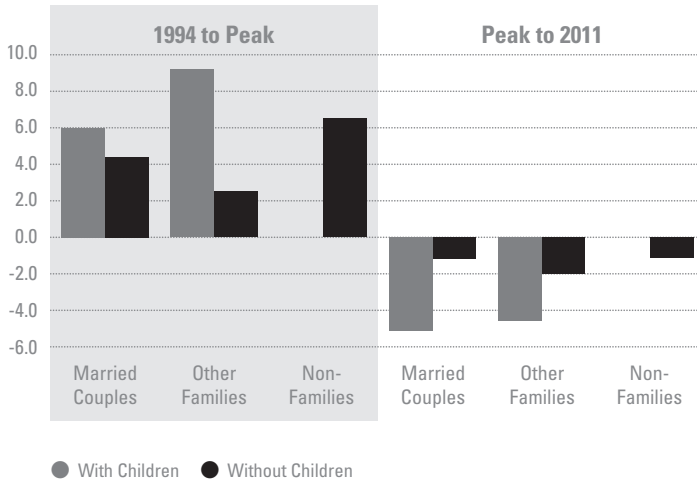
But the stringent credit environment prevents many would-be buyers from taking advantage of lower house prices and rock-bottom interest rates. The Federal Reserve’s survey of senior loan officers reveals that banks tightened underwriting standards every quarter from late 2006 through mid-2010, with very little easing since then (Figure 23). The magnitude and duration of this tightening are unprecedented.

Denial rates for conventional home purchase loan applications reported under the Home Mortgage Disclosure Act reflect these tough credit conditions. While the overall rate rose just two percentage points (from 15 percent to 17 percent) in 2004–10, the increases for specific types of loans and types of borrowers are much larger. In fact, loan application denial rates for Hispanics were up eight percentage points (from 19 percent to 27 percent) over this period, while those for blacks jumped 15 percentage points (from 23 percent to 38 percent). In contrast, rates for white borrowers climbed just three percentage points (from 12 percent to 15 percent). The small increase in the overall denial rate reflects the fact that whites made up 52 percent of applicants in 2004 but 67 percent in 2010.

But loan application denial rates tell only part of the story. Many households with potential credit issues may not even apply for mortgages out of concern they will either not qualify or face higher borrowing costs. CoreLogic reports that home purchase lending to borrowers with less than stellar credit has in fact all but ceased. From 2008 to 2011, the volume of home purchase loans to borrowers with credit scores below 620 plunged 93 percent, while that to borrowers above this cutoff was down about 30 percent. The stringency of underwriting standards is also evident in the fact that, despite the exceptionally weak economy, Lender Processing Services characterizes early delinquency rates on loans originated in 2010 and 2011 as among the best on record.

FIGURE 22

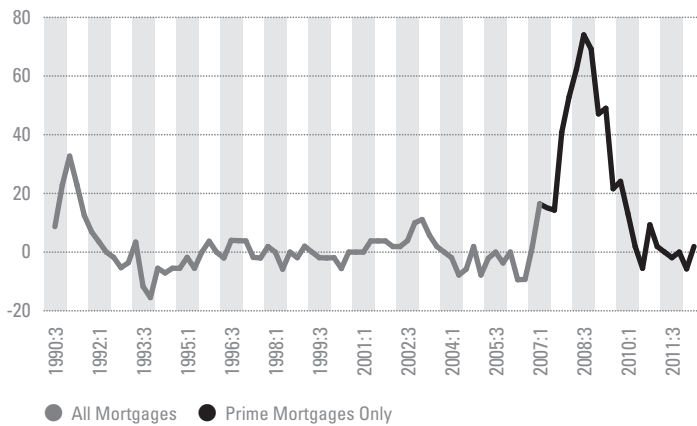
**Families with Children Saw Both the Largest Increase in Homeownership and the Largest Drop Change in Homeownership Rate (Percentage points)**



Notes: The homeownership rate for married couples with children peaked in 2005. Rates for all other categories peaked in 2004. Non-family households are single persons and unrelated individuals without children. Source: US Department of Housing and Urban Development, US Housing Market Conditions, Q4 2011.

FIGURE 23

**Banks Have Sharply Constrained Credit Availability**  
Net Share of Senior Loan Officers Reporting Tighter Mortgage Underwriting Standards (Percent)



Note: The data series for all mortgages was replaced by individual series for prime and subprime loans in 2007. Source: JCHS tabulations of the Federal Reserve Board, Senior Loan Officers Survey.

Even if borrowers with lower credit scores and higher loan-to-value (LTV) ratios are approved for mortgages, they must pay higher interest rates than those making headlines. Beginning in 2008, Freddie Mac and Fannie Mae began to impose additional origination fees on mortgages they purchase or guarantee if the

loans are deemed to pose increased default risk. These fees, or loan level price adjustments (LLPAs), are based on such characteristics as high LTV ratios, low credit scores, minimal mortgage insurance coverage, adjustable interest rates, and subordinate financing. If loans fall into multiple risk categories, LLPAs can represent several percentage points of the loan amount.

Private mortgage insurance is also mandated for loans with LTVs above 80 percent, which may add another \$70–110 monthly for every \$100,000 borrowed, depending on the borrower’s credit standing. Meanwhile, FHA is also raising the cost of its insurance to shore up its balance sheet and encourage more private-sector lending. While necessary, these higher borrowing costs may undermine the ability of some first-time buyers to enter the market.

With their cost advantages, more relaxed underwriting standards, and deep government guarantees that appeal widely to investors, loans insured by the FHA, Veteran’s Administration, and US Department of Agriculture’s Rural Development programs have come to comprise a large share of the home purchase market—particularly among borrowers with small downpayments. From fewer than one in ten during the housing boom, these government-backed loans accounted for more than half of home purchase loans in 2009 and 2010. While expansion of FHA lending has received the lion’s share of attention, funding for USDA’s guarantee loan program also increased five-fold between fiscal 2007 and 2010.

In keeping with their traditional targeting and low-downpayment requirements, government mortgage insurance programs served about two-thirds of low-income homebuyers in 2010. They also guaranteed large shares of home purchase loans to minorities, including 83 percent of black and 76 percent of Hispanic borrowers in that year (Figure 24). Still, more than a third of all higher-income borrowers also opted for such loans, indicating the importance of government guarantees in today’s troubled mortgage market.

**REFINANCING CHALLENGES**

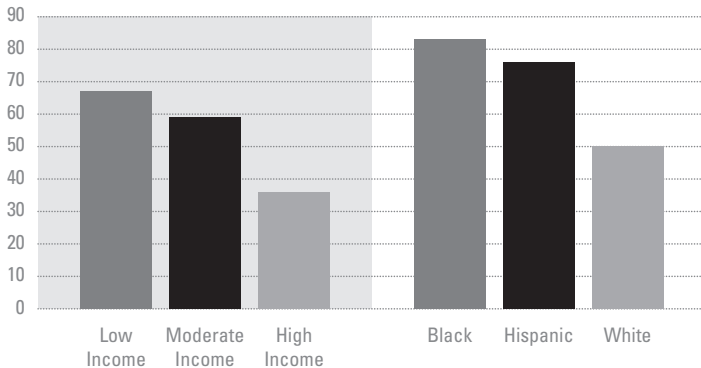
Despite attractive interest rates, refinancing activity edged up only modestly at the end of 2011. In part, the lack of response reflects the fact that many homeowners have already locked in very low rates. But millions of other homeowners who would like to refinance are unable to do so because of impaired income and credit scores, negative equity in their homes, or a combination of the two.

Thus far, government-led refinance assistance programs aimed at credit-impaired or underwater borrowers have focused primarily on households with loans backed by FHA or the GSEs. FHA has long offered a streamlined refinance option allowing borrowers in good standing to take advantage of lower interest rates without a property reappraisal as long as the loan balance does not increase. In the wake

FIGURE 24

### Minorities and Lower-Income Homebuyers Rely Heavily on Government-Backed Loans

Share of Home Purchase Loans with Federal Backing in 2010 (Percent)



Notes: Federally backed loans include FHA/VA and USDA Rural Housing loans. Low income is defined as less than 80 percent of area median income (AMI), moderate income is 80–120 percent of AMI, and high income is above 120 percent of AMI. Black and white householders are non-Hispanic; Hispanics may be of any race. Source: JCHS tabulations of 2010 Home Mortgage Disclosure Act data.

of the foreclosure crisis, FHA relaxed the criteria for these loans, enabling some 720,000 borrowers to refinance into lower rates between April 2009 and the end of March 2012. The Home Affordable Refinance Program (HARP), initiated in 2009, provided a similar option for borrowers with GSE-guaranteed loans that had LTVs above 80 percent. More than one million HARP refinancings were completed by early 2012. Even with these efforts, though, the vast majority of underwater homeowners have been unable to take advantage of historically low interest rates.

Although borrowers with loans up to 125 percent of home values were also eligible for HARP, few had managed to refinance through the program by fall 2011. To reach more distressed homeowners, HARP’s terms were revised late in the year to reduce income and credit screens, lift LTV limits, and free lenders of additional liability from the refinanced loans—a major obstacle to bank participation.

The evidence suggests that refinancing volumes were on the rise as the new guidelines took effect in early 2012. The Congressional Budget Office estimates that HARP could potentially provide a benefit of as much as \$200 per month for as many as 2.9 million homeowners. But for the millions of distressed owners whose loans are not FHA- or GSE-backed, there is still no comparable relief.

#### THE OUTLOOK

Over the next few years, homeownership rates among younger households will remain under pressure. Members of the large echo-boom generation are just beginning to enter the housing market, but primarily as renters. In addition, greater numbers of middle-aged households are delaying homeownership or returning to rental housing. And as millions of distressed homeowners lose their homes to foreclosure, they will require years to repair their tarnished credit records before buying again. As a result, increases in the number of renters will continue to outpace any growth in homeowners. If not for older households, who have high homeownership rates and account for an increasing share of the population, the decline in the national homeownership rate would be much greater.

A strong, sustained economic expansion could, however, produce a quick turnaround—particularly in markets that did not experience the worst of the foreclosure crisis. Buying a home has rarely been more affordable, and a more robust economy would provide the income and confidence that would enable many potential buyers to make the long-term commitment of owning. Indeed, homeownership continues to have strong appeal. In the fourth quarter of 2011, the Fannie Mae survey found that seven out of ten renters—as well as more than eight out of ten homeowners who are underwater on their mortgages—think that owning makes more financial sense than renting.

Young first-time buyers, including an increasing share of minority households, will drive future growth in homeownership. The question going forward is therefore whether the troubled mortgage market will provide access to affordable mortgage credit for borrowers with limited savings and anything but the highest credit ratings.