

# **United States Urban Housing Policy: Supply and Demand for Housing**

## **Future Market Conditions and Policy Implications**

**Presented by**

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**Presented to**

**American Real Estate Society Annual Meeting**

**Coeur d' Alene, Idaho**

**Saturday, April 21, 2001**

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion Topics

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This goals and objective of this paper is to discuss:

- Use historical analysis to identify supply side and demand side housing policy options.
- To test for significance of supply and demand variables for forecast model development.
- To forecast long run supply and demand for housing, and calculate the gap between supply and demand.
- To recommend supply side or demand side policies to bring the market back into long run equilibrium.

## United States Housing Policy

### Supply and Demand for Housing

### Future Market Conditions and Policy Implications

# Discussion- Historical Analysis

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## Historical Analysis of Housing Policy:

### 1850 - 1890

- Despite widespread public recognition of worsening urban housing problems and frequent calls for reform, only after the Civil War were government efforts undertaken to improve housing conditions. *In 1867 the New York state legislature enacted the first tenement-housing legislation, which regulated the construction of railroad flats by establishing minimum construction standards.*

## **United States Housing Policy**

### **Supply and Demand for Housing**

### **Future Market Conditions and Policy Implications**

# **Discussion - Historical Analysis**

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## **Historical Analysis of Housing Policy - *Continued***

1890 – 1930

Attempts to improve housing were spurred by the writings of such reformers as Jacob Riis and Lawrence Veiller in the 1890s, as well as by the first federal report on housing conditions, issued in 1894. Nevertheless, it was not until 1901 that a law permitting enforcement of housing standards was enacted. The landmark New York City "New Law" required building permits and inspections, prescribed penalties for noncompliance, and created a permanent city housing department. Subsequently, the New Law was copied in other U.S. cities and provided an impetus for housing legislation at the state level in the early 1900s.

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**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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## **Historical Analysis of Housing Policy - *Continued***

### *The Depression Era*

With home building almost at a standstill and the rate of foreclosure on home mortgages at an intolerably high level, emergency programs were enacted by the Hoover and Roosevelt administrations to provide jobs in the construction industry, improve housing conditions, and extend financial assistance to people threatened with the loss of their homes.

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **Federal Home Loan Bank System (1932)**

The first major step toward a national housing policy was the creation in 1932 of the Federal Home Loan Bank System, a system of 12 regional banks, supervised by the Federal Home Loan Bank Board. Provides short-term credit to member savings and loan associations. In 1934 the Federal Savings and Loan Insurance Corporation began offering depositors in both federal- and state-chartered associations insurance against the loss of their savings.

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## Discussion - Historical Analysis

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### **Historical Analysis of Housing Policy - *Continued***

#### **National Housing Act (1934)**

The **Federal Housing Administration (FHA)** was created in 1934 as a U.S. government agency whose function was to *insure mortgages*, thus providing banks and other lending institutions with a guarantee that their housing loans would be adequately secured, and the housing industry with a new *stimulus* during a time when almost no new homes were being built. Because FHA-insured mortgages, and the houses they buy, must conform to certain *standards*, the agency has had a great influence on the housing and mortgage-lending industries.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

## Discussion - Historical Analysis

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### **Historical Analysis of Housing Policy - *Continued***

#### **National Housing Act (1934) - *Continued***

FHA revolutionized prevailing mortgage lending practices by developing the level-payment, insured mortgage loan, requiring a small down payment and repayment over 20 or 30 years. Lenders were now willing to participate in the FHA program which insures private mortgage loans on residential property and, by protecting lenders against loss, encourages the use of long-term mortgages with high loan-to-value ratios (Mitchell, 1985).



**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **National Housing Act (1934) - *Continued***

FHA is essentially a government insurance agency that collects premiums from mortgage borrowers and uses them to make good on the losses incurred by lenders because of mortgage foreclosures. Financial institutions are motivated to make more housing loans than they might otherwise. This contributed significantly to reducing mortgage interest rates and the overall cost of housing.

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**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **Housing Act (1937) (U.S. Housing Authority)**

The federal role in housing was further broadened under the Housing Act of 1937, establishing the U.S. Housing Authority (renamed the Federal Public Housing Administration in 1942 and the Public Housing Administration in 1947) as a *permanent agency charged with building and subsidizing local low-income housing projects. This created the basic structure for the nation's system of public housing. More than 1.5 million dwelling units have been erected under this act (Fish, 1979).*

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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*By World War II the federal role in promoting housing construction and stable housing markets had been established, and a burgeoning commitment to low-income housing was evolving.*

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

**Federal National Mortgage Association (FNMA, or "Fannie Mae") (1948)**

Became a private organization in 1968. Provides a secondary market for FHA and Veterans Administration (VA) home mortgage loans by standing ready to purchase such loans from financial institutions.

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **Housing Act (1949)**

Created the **Urban Redevelopment Agency** and gave it the authority to subsidize three fourths of the cost of local slum clearance and urban renewal. Under the act, "primarily residential" and "blighted" urban areas could be condemned, cleared of buildings, and sold for private redevelopment. This legislation established the goal of providing decent homes for all U.S. households (Fish, 1979).

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**  
**Discussion - Historical Analysis**

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**Historical Analysis of Housing Policy - *Continued***

**Housing and Urban Development Act (1965)**

Established the Cabinet-level **Department of Housing and Urban Development (HUD)**. HUD was formed from the Housing and Home Finance Agency (HHFA) and incorporated the Federal Housing Administration, the Federal National Mortgage Association, the Public Housing Administration, the Urban Renewal Administration, and the Community Facilities Administration (Mitchell, 1985).

**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **Demonstration Cities and Metropolitan Development Act (1966)**

The Model Cities Program of 1966 sought to solve the education, employment, welfare, and health problems of slum dwellers as well as their housing problems.

#### **Housing and Urban Development Act (1968)**

A principal objective of the Housing and Urban Development Act of 1968 was to encourage the creation of "New Communities."

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**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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## **Historical Analysis of Housing Policy - *Continued***

### **FNMA 1968**

The **FNMA and the Government National Mortgage Association ("Ginnie Mae")**, created in 1968 as a counterpart to "Fannie Mae," assist the housing industry by purchasing FHA and VA mortgages



**United States Housing Policy**

**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

## **Discussion - Historical Analysis**

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### **Historical Analysis of Housing Policy - *Continued***

#### **Housing and Urban Development Act (1970)**

Authorized greater outlays for housing subsidy programs and additional funds for rent supplements to moderate-income households.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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## **Historical Analysis of Housing Policy - *Continued***

### **Emergency Home Finance Act (1970)**

Authorized the Home Loan Bank System to reduce interest rates on home mortgages by means of a federal subsidy. Established mechanisms for a secondary market in conventional mortgages through the creation of **the Federal Home Loan Mortgage Corporation (FHLMC)**. Created a special interest subsidy program for low- and moderate-income housing.

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**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**  
**Discussion - Historical Analysis**

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**Historical Analysis of Housing Policy - *Continued***

**Equal Credit Opportunity Act (1974)**

Prohibited discrimination in credit transactions, such as applying for a mortgage loan, on the basis of sex or marital status (Fish, 1979).

## **United States Housing Policy**

### **Supply and Demand for Housing**

### **Future Market Conditions and Policy Implications**

# **Discussion - Historical Analysis**

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## **Historical Analysis of Housing Policy - *Continued***

### **The Housing and Community Development Act (1974)**

This act sharply reduced new construction subsidies and shifted the emphasis for low-income housing to the use of (Section 8) leased-housing allowances and vouchers for renting already existing housing. Under the Section 8 program, low-and moderate-income families pay up to 30 percent of their income for rent, HUD pays difference, rent ceiling are established to control cost. This act liberalized the types and amounts of loans a savings association may make, and consolidate urban renewal and model cities programs into block grants.

## United States Housing Policy

### Supply and Demand for Housing

### Future Market Conditions and Policy Implications

# Discussion - Historical Analysis

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## **Historical Analysis of Housing Policy - *Continued***

### 1980s

Federal spending dramatically reduced under President Reagan; the net budget authority for public housing and subsidized rentals dropped from about 28 billion dollars in 1980 to about 9 billion dollars in 1989, despite an increase in poverty-level households. During the same period the Department of Housing and Urban Development (HUD) was wracked by political favoritism, fraud, and misuse of funds totaling as much as 4 billion dollars. Both trends were reversed starting in 1989 under HUD secretary Jack Kemp and led to 1990 legislation funding construction, rehabilitation, and tenant ownership of public housing (Bratt-Rachel, 1993).

## **United States Housing Policy**

### **Supply and Demand for Housing**

### **Future Market Conditions and Policy Implications**

# **Discussion - Historical Analysis**

## **US Housing Policy Analysis**

### **Demand-Side Policy Tools:**

Subsidies: direct cash payments, housing allowances or vouchers, or preferential homeownership tax treatment. In the U.S., the largest subsidy comes in the form of preferential tax treatment of mortgage interest payments, as opposed to Section 8 vouchers.

### **Supply-Side Policy Tools**

Supply-side subsidies go to suppliers of housing and reduce the costs of provision. These subsidies reduce the cost of providing housing by builders and landlords. Subsidies can take the form of direct cash payments, fiscal concessions on taxes, reductions in loan payments, subsidized mortgage interest rates, loan underwriting warranties, or land grants for development (Vliet, 1998).

## **United States Housing Policy**

### **Supply and Demand for Housing**

### **Future Market Conditions and Policy Implications**

# **Discussion - Historical Analysis**

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## **US Housing Policy Analysis**

### **Predominant Policy Bias**

Since 1840 the U.S. government policies toward housing has been biased toward supply-side incentives. In almost every case of legislation, the policy bias has been toward increasing housing production. The only periods in which there is demand-side bias is during depressions and recessions.

- A significant portion of supply-side legislation comes in the form of direct subsidies to low-income residents and grants to affordable housing developers.
- The majority of supply-side legislation takes the form of banking or finance subsidies or loan guarantees to developers and individuals.

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**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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## Legislative Analysis

### *Supply-Side Legislation (Construction and Lending)*

- Federal Home Loan Bank System (1932)
- Home Owner's Loan Corporation (1933)
- Resettlement Administration (1933)
- National Housing Act (1934)
- Housing Act (1937)
- Servicemen's Readjustment Act (1944)
- Farmers Home Administration (1946)
- Federal National Mortgage Association (1948)
- Housing Act (1949)
- Housing Act (1954)
- Housing Act (1964)
- Housing and Urban Development Act (1965)
- Demonstration Cities and Metropolitan Development Act (1966)
- Housing and Urban Development Act (1968)
- Housing and Urban Development Act (1970)
- Emergency Home Finance Act (1970)
- Equal Credit Opportunity Act (1974)
- Tax Reform Act of 1986
- National Affordable Housing Act of 1990



**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion - Historical Analysis

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## Legislative Analysis

### *Demand-Side Legislation (Employment and Buying Power)*

- The Public Works Administration (1933)
- Housing and Community Development Act (1974)
- Housing and Community Development Act (1977)

As shown in the model forecast section, housing supply in the U.S. will continue to outstrip housing demand.

Housing supply will continue to exceed housing demand due to a federal housing policy bias toward supply-side legislation.

**United States Housing Policy**  
**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

**Discussion – Quantitative Analysis**

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**Data Collection:**

- U.S. Department of Commerce, Bureau of the Census
- Federal Reserve System
- U.S. Department of Labor
- National Association of Realtors
- Construction Industry Board
- Department of Housing and Urban Development (HUD)
- Columbia University Center for Business Cycle Research
- Etc.

## **United States Housing Policy**

### **Supply and Demand for Housing**

#### **Future Market Conditions and Policy Implications**

# **Discussion – Quantitative Analysis**

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## **Demand Factors**

Housing demand is a preference for housing services subject to constraints of income and price. The household is the basic unit of housing demand, and as defined by the U.S. Census.

Determinants of household formations are the number of total households, economic and demographic characteristics, tastes and preferences, prices of substitute and complementary goods, and expectations (Carn, 1988).

**United States Housing Policy**  
**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

**Discussion – Quantitative Analysis**

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**Demand Factors**

Demographic factors affecting housing demand are: rate of household formations, size and age-mix of population, and household size. Other factors affecting housing demand are inflation and deterioration (Marcin, 1975).

Other factors important to determining demand for housing services are: permanent income, marginal tax rate, income growth, expected rate of return on housing, family size and location of home (Haurin, 1989).

**United States Housing Policy**  
**Supply and Demand for Housing**

**Future Market Conditions and Policy Implications**

**Discussion – Quantitative Analysis**

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**Demand Factors**

Factors contributing to home price appreciation rates are: cost inflation, employment growth, real income growth, and change in interest rates (Abraham and Hendershott, 1996).

Housing demand is the quantity of housing desired by households individually and in aggregate. Housing demand is negatively related to the price of housing, and positively related to household income. As the price of housing falls due to lower interest rates, construction costs or real tax burdens, the demand for housing, or household formations, increase (Pozdena, 1988).

## **United States Housing Policy**

### **Supply and Demand for Housing**

#### **Future Market Conditions and Policy Implications**

# **Discussion – Quantitative Analysis**

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## **Supply Factors**

Housing supply can be thought of as stock of units, flow of services or quality of accommodations from the stock. The census, estimates that there are over 102.3 million dwelling units in the U.S.

Housing supply is not easy to determined due to the difficulty of assessing and measuring the supply of available land for development. But it is assumed that in the long run housing supply is infinite, and that developers will find a higher and better use of the land, and if that means building up or tearing down an existing structure, they will.

## **United States Housing Policy**

### **Supply and Demand for Housing**

#### **Future Market Conditions and Policy Implications**

# **Discussion – Quantitative Analysis**

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## **Supply Factors**

It has been found that housing construction is determined by roughly six factors: level of historical housing starts, rate of household formations, rate of removals, number of vacant units, rent growth, and interest rates (Smith, 1970).

Rapid home price appreciation, above construction costs, give developers incentive to produce more housing, but before developers will develop, they must be convinced that consumers are confident enough in the current employment and economic environment (Weber and Devaney, 1996). The market for new homes depends partly on consumer attitudes and perceptions embodied in consumer confidence indices.

## **United States Housing Policy**

### **Supply and Demand for Housing**

### **Future Market Conditions and Policy Implications**

# **Discussion – Quantitative Analysis**

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## **Supply Factors**

The true relationship between private housing starts and the economy is a function of the money supply and overall performance of national output measured by GDP. Historically, it has been shown that growth of deposits at savings and loans was a significant determinant of housing starts in 1966 and 1971, but not in other years (Johnson, 1982).



## United States Housing Policy

### Supply and Demand for Housing

### Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

## Supply Factors

Factors showing strong correlation with housing supply are: 1970 - 1999

- CPI growth (-9)
  - Consumer confidence (-1)
  - Absolute change in GDP (0)
  - Change in home prices (-5)
  - Interest Rates (0)
  - Affordability (0)
- 
- Note: Data are year-over-year quarterly changes changes.
  - Numbers in parentheses are the number of lagged periods.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Supply Factors

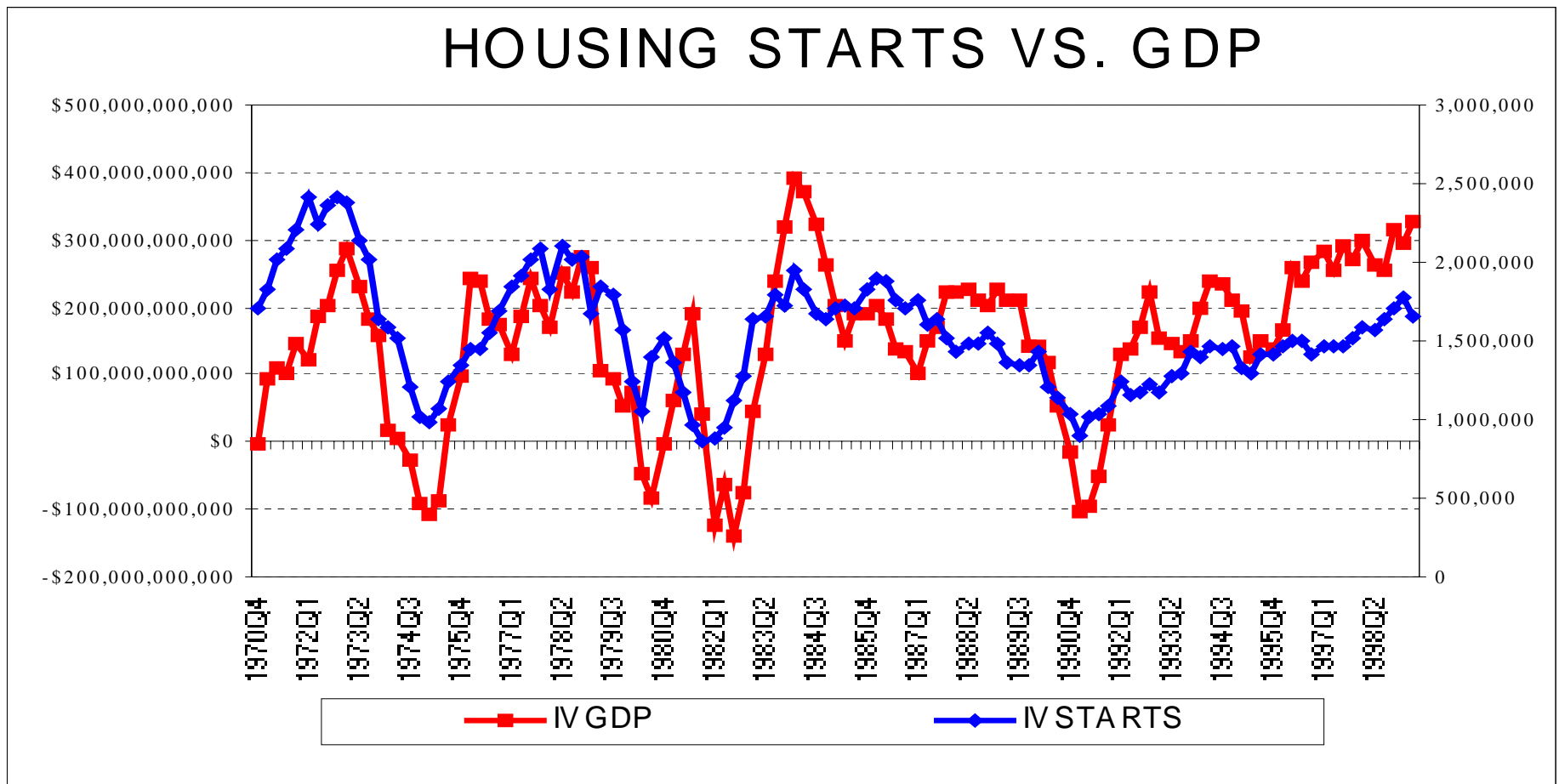
Demand Variables	Correlation	
	Coef.	t Stats
YOY Ann. Absolute Change GDP (0)	52.59%	6.57
YOY Ann. Absol.Change Housing Inventory (-4)	42.38%	4.97
Rolling Ann.Qtr. Avg.10 year Int. Rts.(0)	28.56%	-3.17
YOY Ann. % Change Personal Income Per Household (-3)	47.98%	5.81
Rolling Ann.Qtr. Avg.Housing Affordability Index (0)	28.17%	3.07
YOY Ann. % Change CPI Ndx. (-9)	57.50%	7.47
YOY Ann. % Change Home Price (-5)	49.91%	6.12
YOY Ann. % Change Consumer Confidence Index (-1)	57.39%	6.49
Rolling Ann.Qtr. Avg.Home Sales (0)	2.47%	0.26
Rolling Ann.Qtr. Avg.Single-Family Starts (0)	79.40%	13.88
Rolling Ann.Qtr. Avg.Multifamily Starts (0)	84.84%	17.04

# United States Housing Policy Supply and Demand for Housing

## Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

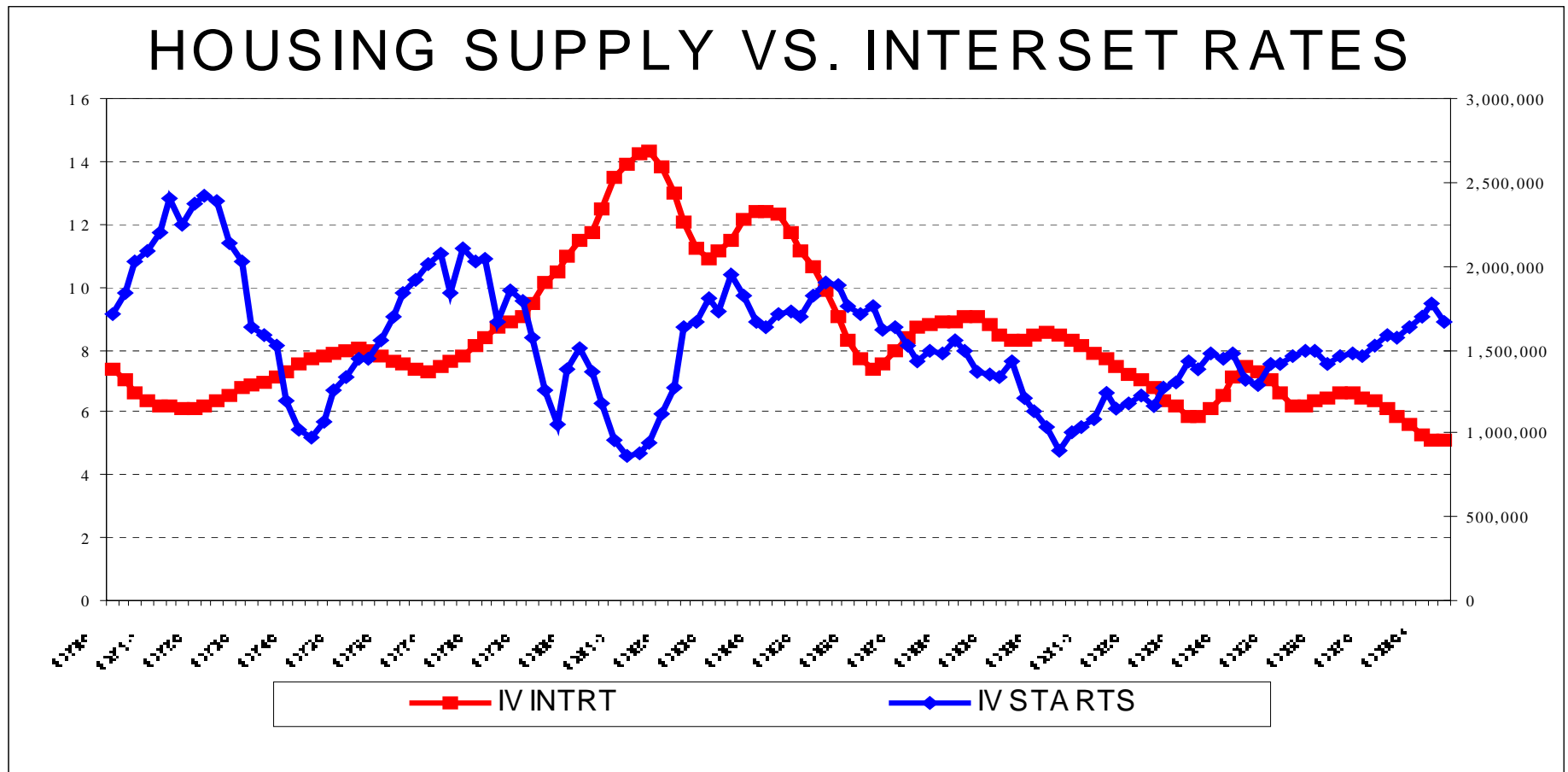
## Supply Factors - *Continued*



**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Supply Factors - *Continued*



**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Demand Factors

Factors showing strong correlation with housing demand are:

- Number of persons per household (0)
  - Home price appreciation (0)
  - Income per household growth (-2)
  - Inflation rate (0)
  - Employment growth (-1)
- 
- Note: Numbers in parentheses are the number of lagged periods.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

**Discussion – Quantitative Analysis**

**Demand Factors**

Demand Variables	Correlation	
	Coef.	t Stats
YOY Ann. Absolute Change GDP (0)	15.70%	1.69
<b>YOY Ann. Change EMPLOY (-1)</b>	<b>21.50%</b>	<b>2.33</b>
<b>Rolling Ann.Qtr. Avg.UNEMP (-1)</b>	<b>17.63%</b>	<b>-1.91</b>
YOY Ann. Change POP24-65 (0)	10.10%	1.07
<b>Number of Persons Per Hhld. (0)</b>	<b>61.70%</b>	<b>8.33</b>
<b>YOY Ann. % Change Personal Income Per Household (-2)</b>	<b>51.90%</b>	<b>6.45</b>
Rolling Ann.Qtr. Avg.Housing <b>Affordability Index (-0)</b>	<b>22.53%</b>	<b>2.41</b>
<b>YOY Ann. % Change Home Price (0)</b>	<b>57.01%</b>	<b>7.37</b>
Rolling Ann.Qtr. Avg.10 year Int. Rts.(0)	13.75%	-1.47
<b>YOY Ann. % Change CPI Ndx. (0)</b>	<b>28.09%</b>	<b>3.11</b>

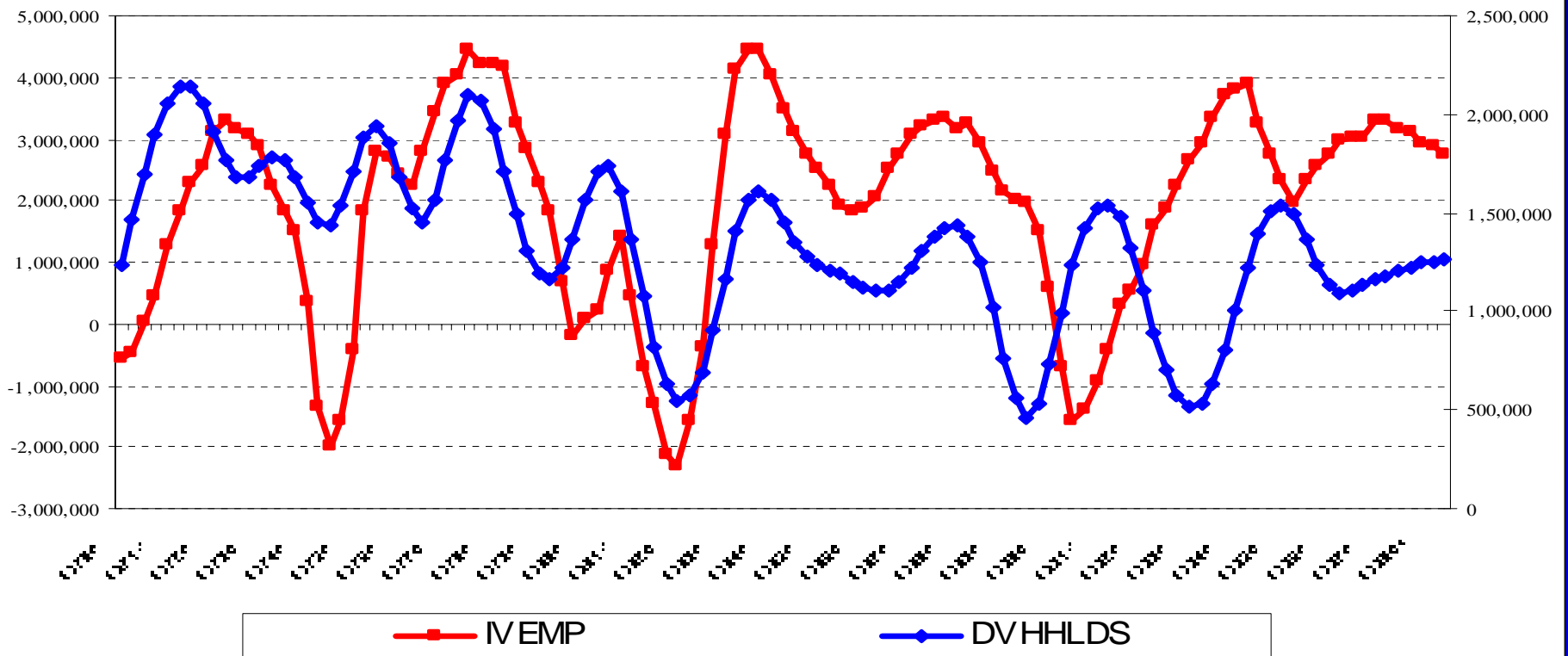
# United States Housing Policy Supply and Demand for Housing

## Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

## Demand Factors - *Continued*

### HOUSING DEMAND VS. EMPLOYMENT



Source: U.S. Department of Commerce, Federal Reserve, U.S. Bureau of the Census.

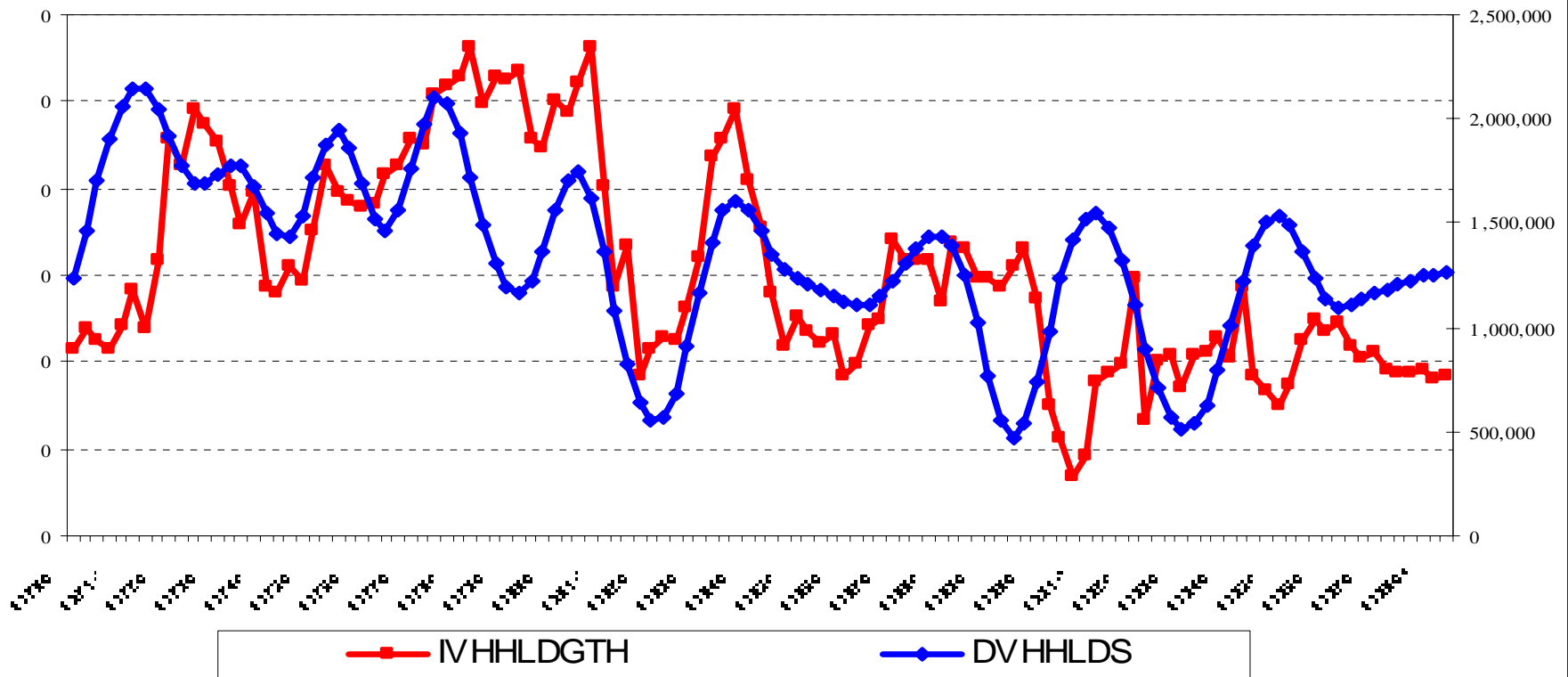
# United States Housing Policy Supply and Demand for Housing

## Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

## Demand Factors - *Continued*

### HOUSING DEMAND VS. INC. PER HHLD



Source: U.S. Department of Commerce, Federal Reserve, U.S. Bureau of the Census.



**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Supply and Demand Model Results

- **Reduced Form - Supply Model Forecast Equation**
- Of the significant supply variables, change in GDP, change in housing inventory lagged four periods, interest rates and inflation lagged nine periods produced a statistically significant forecast model and adheres to economic theory. This model was then used to forecast future housing supply.

- 
- $$DVSTARTS = 975,792 + 1.44 (IVGDP(0)) + 0.11 (HOUSINGINV(-4)) +$$
- $$-14,269 (IVINTRT(0)) + 5,528,833 (IVCPI(-9))$$
- $$[8.16] \qquad [4.06]$$
- $$[-1.53] \qquad [8.86]$$
-

- **Multiple R = 82%**      **R Square = 67%**      **Adj. R Square = 66%**      **F Stat = 55.7**

- Note: Numbers in brackets are “t” statistics; and numbers in parentheses are number of lagged periods. Regression was run at a 90% confidence level.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Supply and Demand Model Results

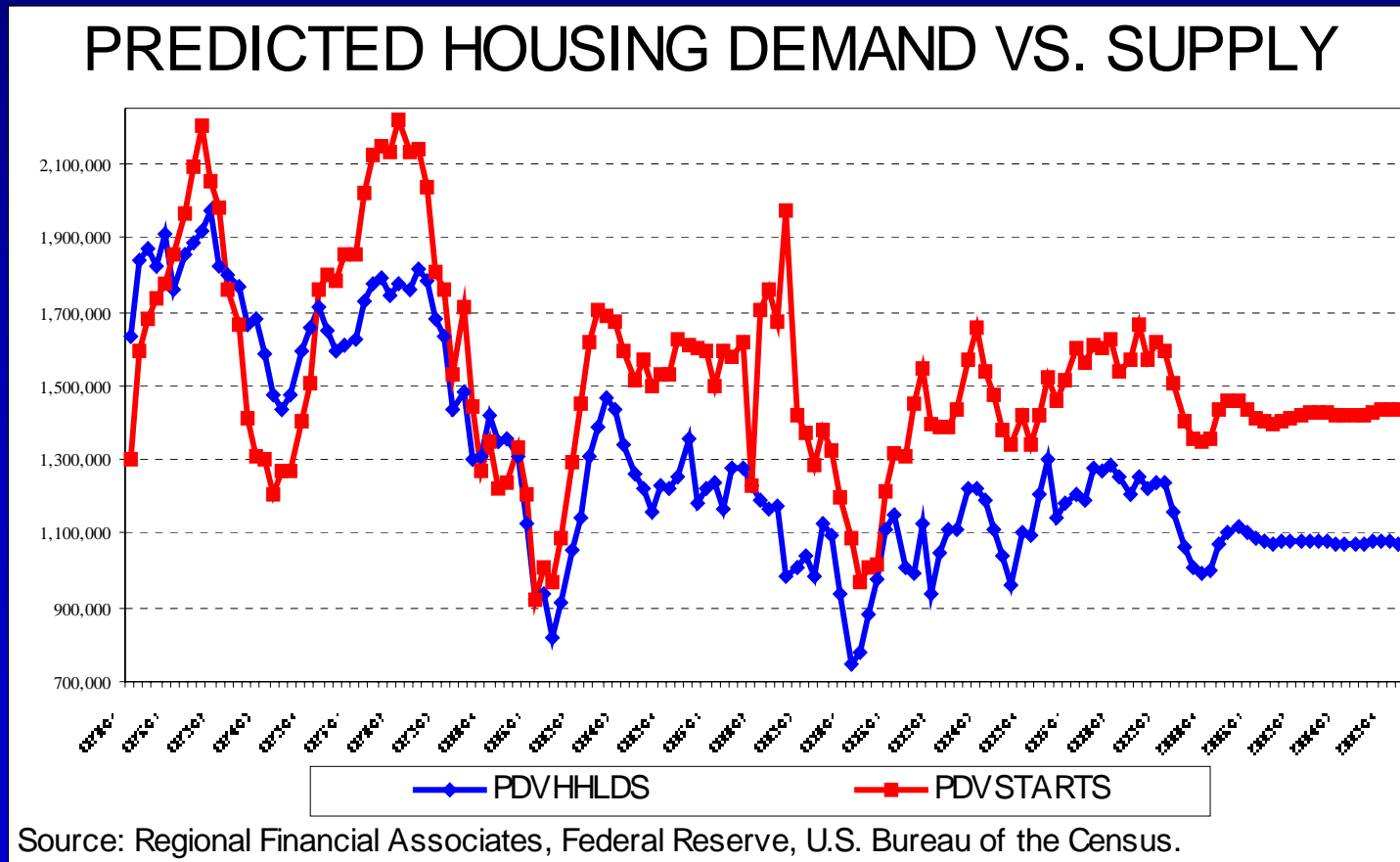
- **Reduced Form - Demand Model Forecast Equation**
- 
- Of the significant demand variables, change in GDP, change in number of persons per household, and home sales price appreciation produced a statistically significant forecast model and adheres to economic theory. This model was then used to forecast future housing demand.
- 
- $DVHHLDS = -2,923,272 + 1.05 (IVGDP(0)) + 1,374,827 (IVPERSPERHHLD(0)) +$   
[4.70] [6.86]
- 
- $3,654,143 (IVSAL$GTH(0))$   
[-1.53]
- 
- Multiple R = 75%      R Square = 56%      Adj. R Square = 55%      F Stat = 46.9

# United States Housing Policy Supply and Demand for Housing

## Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

## Supply and Demand Gap Analysis

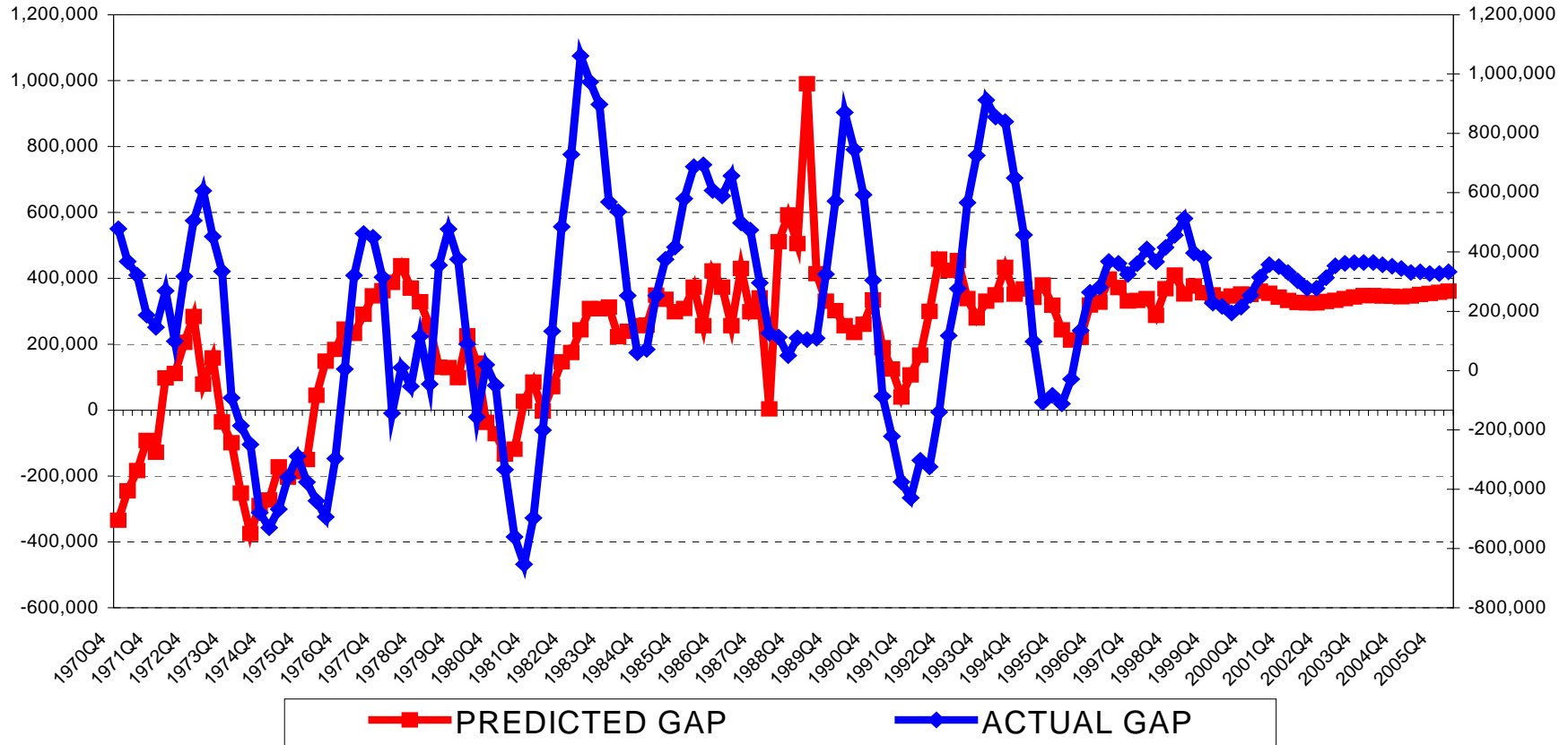


# United States Housing Policy Supply and Demand for Housing

## Future Market Conditions and Policy Implications

# Discussion – Quantitative Analysis

## PREDICTED VS. ACTUAL HOUSING GAP



Source: Regional Financial Associates, Federal Reserve, U.S. Bureau of the Census.

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Discussion – Quantitative Analysis

## Supply and Demand Gap Analysis

Based on the housing gap analysis:

- From 1999 through 2027, the gap between housing supply and demand will grow from 350,000 units per year to 480,000 units per year. This is an average annual compound growth rate over the twenty-eight year period of roughly 1.0% per year.
- The continuation of this housing gap is a reflection of expansionary fiscal housing policy, and its effect should be reflected in declining rates of real-home prices and higher housing affordability over the twenty-eight years.

# United States Housing Policy

## Supply and Demand for Housing

### Future Market Conditions and Policy Implications

# Conclusion

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The federal government has acted to make mortgage funds more readily available, its direct role in housing finance has diminished markedly. In the past, federal policy actions have been of four different types:

- 1) those which provide the framework and support for housing finance markets;
- 2) those aimed at under housed segments of the population;
- 3) those which respond to crisis situations, for example, the creation of the HOLC in the 1930s;
- 4) those which encourage housing production generally--such as the mortgage interest and real-estate tax deductions allowed to homeowners.

Some federal legislation aimed at non-housing problems, such as programs to improve urban transportation and environmental quality, have had substantial impact on the cost, location, and quality of residential structures.

Together with general economic growth, federal supply-side housing policies have been successful in nearly eradicating the worst housing problems of previous decades.

# United States Housing Policy

## Supply and Demand for Housing

### Future Market Conditions and Policy Implications

## Conclusion

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In the future, housing supply in the U.S. will continue to outstrip housing demand. Housing supply will continue to exceed housing demand due to a federal housing policy bias toward supply-side legislation.

Factors showing strong correlation with housing supply over the years are:

- Single and multi-family housing starts
- Historical Change in housing inventory
- CPI growth
- Consumer confidence
- Absolute change in GDP
- Change in home prices
- Interest Rates
- Affordability

**United States Housing Policy**  
**Supply and Demand for Housing**  
**Future Market Conditions and Policy Implications**

# Conclusion

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From 1999 through 2027, the gap between housing supply and demand will grow from 350,000 units per year to 480,000 units per year. This is an average annual compound growth rate over the twenty-eight year period of roughly 1.0% per year.

The continuation of this housing gap is a reflection of expansionary fiscal housing policy, and its effect should be reflected in declining rates of real-home prices and higher housing affordability over the twenty-eight years.



# United States Housing Policy

## Supply and Demand for Housing

### Future Market Conditions and Policy Implications

# Conclusion

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## Recommendations

The downside to supply-side policies is environmental degradation and urban sprawl. To take environmental conditions into consideration, the federal government should look at including “smart growth” incentives. These incentives would channel housing development to existing infill or central city locations.

Other policy recommendations are to eliminate or reduce mortgage interest deductions, reduce subsidized mortgage finance operations, and scale back on government warranties.

Due to current policies in place, the housing market in the U.S. is exposed to oversupply conditions in the future. Although, market oversupply is a risk to developers and property owners, it is a benefit to consumers due to lower prices and higher levels of affordability.

Federal housing policy is supply-side biased, and produces supply bubbles, because it benefits the general public. Overall, U.S. housing policy is effective in increasing homeownership, housing supply, construction quality, and living conditions.