Upper-Income, Educated, Married with Children, and Still Not Buying: Declining Homeownership among "Prime" First-Time Home Buying Candidates

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"The homeownership rate of prime first-time home buying candidates was lower in 2012 than it was in 2000, prior to inflation of the mortgage credit bubble."

Introduction

Homeownership among young adults fell sharply during the housing bust, accelerating a long-term trend that saw the homeownership rate of householders under age 35 decline by nearly 11 percentage points between 1980 and 2012. This is compared with a drop in the overall homeownership rate of less than 1 percentage point during the same period. Recent research suggests that long-running social and demographic shifts, including delayed marriage and child bearing, and increased racial and ethnic diversity among young adults, account for much of the decrease. Short-term cyclical changes, such as the recession-induced rise in unemployment and decline in real household incomes among young adults, have hastened the pace of homeownership decline in recent years.

This edition of *Housing Insights* shows that homeownership rates have fallen substantially among young adults even *after* controlling for key demographic, social, and economic attributes. It is true that long-term demographic and social change and the recent economic downturn contributed to young adults' declining homeownership. However, these factors do not fully explain the decline in homeownership rates. Specifically, this analysis shows that the homeownership rate of "prime" first-time home buying candidates – upper-income households with householders[1] in their early 30s who have college educations and are married with children – fell by 8.6 percentage points between 2006 and 2012, compared with a 3.4 percentage point decline in the overall homeownership rate during the same period. The homeownership rate among prime first-time home buying candidates not only has fallen below what was likely an unsustainable level at the peak of the housing bubble, but it also is now substantially lower than in 2000, before the widespread easing of lending terms that accompanied the mortgage credit boom. The analysis also shows that the homeownership rate dropped for prime first-time home buying candidates who are non-Hispanic white alone.

These findings do not dismiss long-run demographic and social shifts and short-run macroeconomic change as important factors shaping homeownership trends among young adults. Rather, the decline in homeownership among prime first-time home buying candidates suggests that other factors such as the rolling back of loose mortgage lending standards from the housing boom, the recent rash of foreclosures, and uncertainty regarding future incomes and house prices might also be suppressing homeownership among young adults.

Defining "Prime" First-Time Home Buying Candidates

Recent analyses by Jed Kolko and Richard Green used multivariate techniques to assess the influence of demographic, social, and economic factors on homeownership trends among young adults.[2] Kolko concluded that the homeownership decline among 18-34 year-olds over the last two decades is almost completely attributable to shifts in the composition of the young adult population along the dimensions of sex, race,

[1] A householder is typically the person, or one of the persons, in whose name the housing unit is owned, being bought, or rented.
[2] Jed Kolko, "The Recession's Lost Generation of Homeowners Isn't Millennials – It's the Middle-Aged," *Trulia Trends*, July 16, 2014, http://www.trulia.com/trends/2014/07/recessions-lost-generation/. Richard Green, "Young People Are Less Likely to Be Homeowners – In Large Part Because They Are Not Getting Married," *Forbes*, June 14, 2014, http://www.forbes.com/sites/richardgreen/2014/06/14/young-people-are-less-likely-to-be-homeowners-and-it-is-not-just-because-they-are-not-getting-married/.

ethnicity, foreign-born status, family status, educational attainment, and school enrollment. Green examined a similar set of factors, concluding that demographic and social shifts – and particularly delayed marriage – explain the decline in young homeownership, although he did find that these shifts did not fully account for the drop in homeownership among young adults in their 30s.[3]

This *Housing Insights* takes a different approach from the aforementioned multivariate analyses, focusing instead on homeownership trends for a single stratum of young adults who should be "prime" candidates for first-time homeownership (see Exhibit 1). This approach not only controls[4] for several of the key determinants of homeownership examined by Kolko and Green, but it also provides an explicit focus on a subset of young adults who should have high homeownership propensities by virtue of their affluence (household incomes above $95,000 in 2012 dollars), educational attainment (the householder holds a bachelor's or higher degree), and nuclear family status (households consisting of married couples with minor children).[5]

Exhibit 1. Characteristics of "Prime" First-Time Home Buying Candidates

Characteristic	Description and Justification
30 to 32 year-old householder	According to the National Association of Realtors'® annual *Profile of Home Buyers and Sellers*, the median age of first-time home buyers ranged from 30 to 32 years old between 2006 and 2012.
College-educated householder	"College-educated" indicates completion of at least a Bachelor's degree. Greater educational attainment is associated with higher permanent income, which in turn is associated with higher homeownership rates. Some studies also have used educational attainment as a proxy for family wealth, which could overcome the down payment constraint of home purchase.
Nuclear-family household	"Nuclear-family" indicates households composed of a married couple with at least one own child. (An "own child" is a never-married child under 18 years old who is a son or daughter by birth, a stepchild, or an adopted child of the householder.) Nuclear-family households are assumed to be "demographically" motivated to buy. Nuclear families might prefer owner-occupied housing because they are less mobile, and thus able to spread the higher transaction costs of owner-occupied housing over more years; because owner-occupied housing might be perceived as providing greater residential stability, security, and other characteristics suitable for raising a family; or because nuclear families are typically larger than other household types, thus making the larger single-family units that dominate the owner-occupied stock more appealing.
Upper-income household	"Upper-income" means households that have pre-tax money incomes in the top quartile of the income distribution for all households in 2006, the year in which homeownership rates peaked in the Census Bureau's American Community Survey. To identify upper-income households in other years, the 2006 top quartile dollar value cutoff was adjusted for inflation using the consumer price index for all urban consumers research series. In 2012, the upper-income cutoff was $95,245. The positive association between income and homeownership might arise for several reasons. First, the tax benefits of homeownership increase with higher income. In addition, the lower transaction costs of renting should be appealing to lower-income households, who tend to be more mobile. Finally, the relatively higher cost of owner-occupied housing is more affordable to households with upper incomes.

For selected components of the analysis, this *Housing Insights* identifies additional subgroups within the prime first-time home buying group. Prime home buying candidates who are non-Hispanic white alone are examined separately to control for the shift in the composition of young adults toward racial and ethnic minorities, who tend to have lower homeownership rates. Recent movers (households in which the householder lived in a different location one year prior to the interview) also are isolated in some parts of the analysis to explore the tenure choices of households who have recently been in the housing market.[6]

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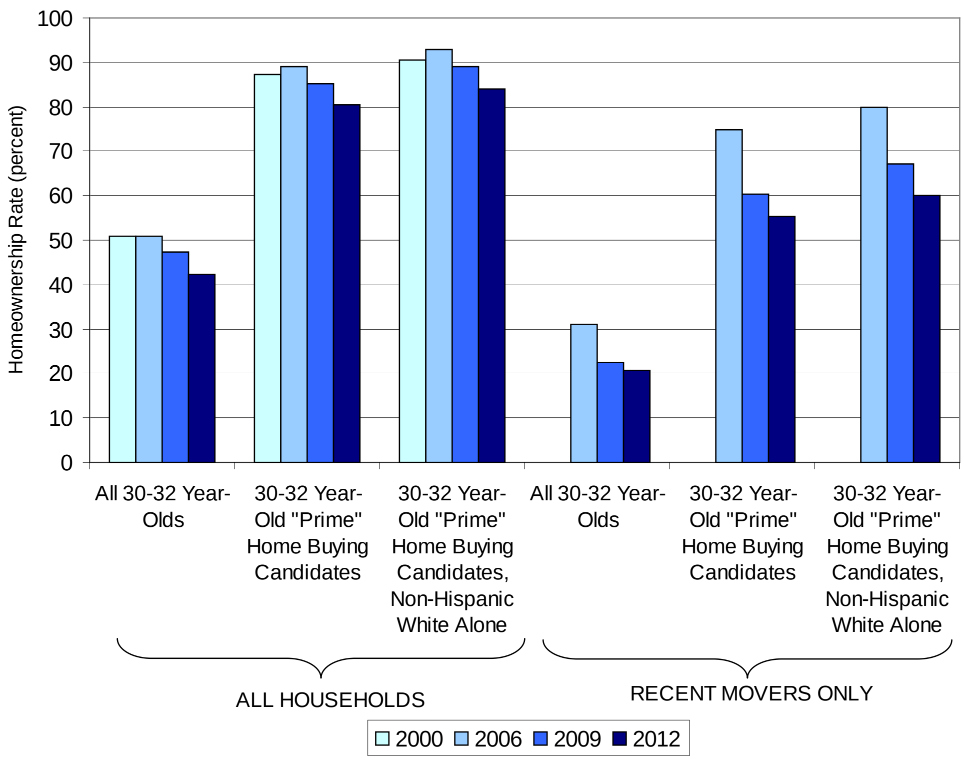
[3] In addition to accounting for most of the demographic and social characteristics of Kolko's analysis, Green also controls for income change.
[4] These controls are admittedly simple in that they do not account for all of the factors that might affect homeownership rates. For example, some analyses of homeownership attainment have examined the effects of foreign-born status and school enrollment. In addition, shifts in the distribution of households within the upper-income and college-educated groups (for example, shifts to lower incomes within the broad upper-income quartile or increases in the proportion of college-educated adults who go on to obtain higher degrees) could lead to changes in homeownership rates. With respect to the potential effects of school enrollment and foreign-born status, the percent of prime first-time home buying candidates who were enrolled in school or foreign-born did not change significantly between 2006 and 2012.
[5] A few of the multiple studies that have discussed the positive associations between the homeownership rate and income, educational attainment, and nuclear family status include Donald R. Haurin, Christopher E. Herbert, and Stuart S. Rosenthal, 2007, "Homeownership Gaps Among Low-Income and Minority Households," *Cityscape* (9, 2): 5-51; Gary Painter, Stuart Gabriel, and Dowell Myers, 2000*, The Decision to Own: The Impact of Race, Ethnicity, and Immigrant Status*, Research Institute for Housing America, Working Paper 00-02; and N. Edward Coulson, 1999, Why are Hispanic- and Asian-American Homeownership Rates So Low?: Immigration and Other Factors, *Journal of Urban Economics* (45): 209-227.
[6] Recent movers are by definition more mobile than all households, and hence have a greater likelihood of being renters.

Young Homeownership Rate Drops Substantially, Even Among Prime First-Time Home Buying Candidates

Prime first-time home buying candidates are very likely to own their homes, but their homeownership rates have fallen substantially in recent years, as shown in Exhibit 2. Between the housing market peak in 2006 and the most recent year of American Community Survey data in 2012, the homeownership rate of prime home buying candidates fell by 8.6 percentage points, the same decline experienced by all 30-32 year olds.[7] Not only was the 2012 homeownership rate for prime first-time home buying candidates lower than in 2006, when easy credit and the house price bubble led to inflated purchasing activity, but it also was nearly 7 percentage points below the rate recorded in 2000, prior to the easing of loan qualification terms during the mortgage “credit bubble.”[8] In addition, rates declined by approximately 6 percentage points between 2000 and 2012 for prime first-time home buying candidates who are non-Hispanic white alone (third set of bars in Exhibit 2), indicating that racial and ethnic shifts do not explain all of the decline in homeownership attainment among young adults who are good candidates for first-time homeownership.

Exhibit 2. Homeownership Has Fallen Even Among Young Adults Who Are "Prime" Home Buying Candidates



Source: U.S. Census Bureau, 2000 Census and American Community Survey Public Use Microdata Samples
Note: Data for recent movers are not available for 2000 because the 2000 Census did not ask about residence one year ago.

At any point in time, the homeownership rate for a given population group reflects the accumulation of past tenure choices made over the course of multiple years and under a variety of housing and economic conditions. For example, the homeownership rate for 30 to 32 year-olds in 2009 not only reflected recent movers’ housing choices, which were made in the midst of one of the most severe economic and housing downturns in recent memory, but also the tenure choices of households who moved years earlier during an economic expansion, homeownership boom, and house price bubble.

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[7] Unless otherwise noted, all differences or changes noted in the text are statistically significant at the 90 percent confidence level.

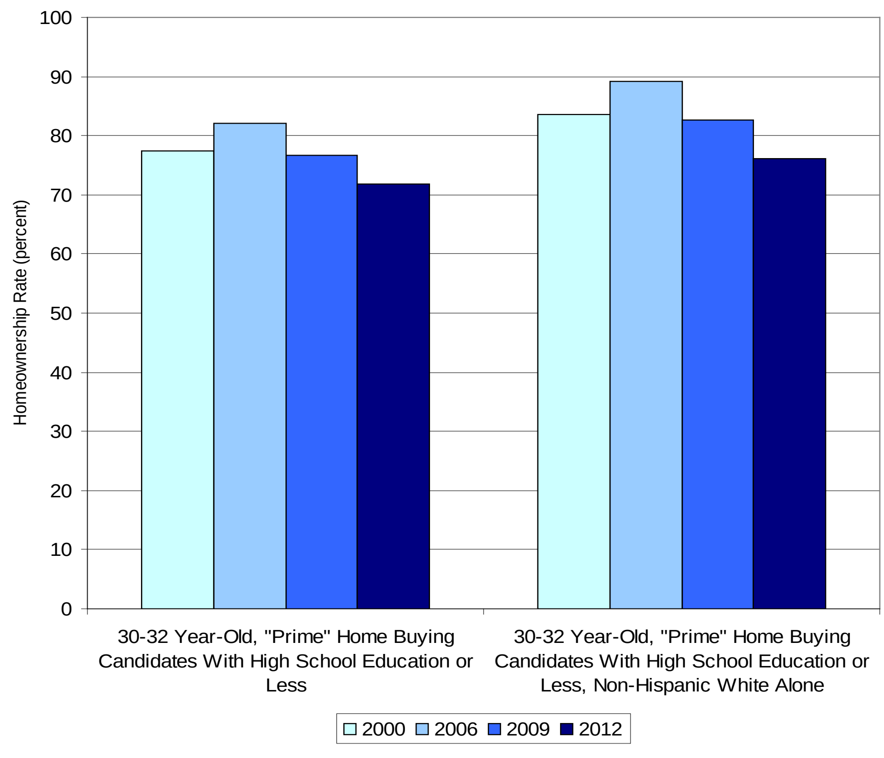
[8] For an account of how the residential “credit bubble” inflated during the first half of the 2000s and helped to promote increases in homeownership and fuel the housing boom, see Financial Crisis Inquiry Commission, *The Financial Crisis Inquiry Report*, U.S. Government Printing Office, January 2011. The Report discusses growth in subprime and Alt-A lending and the proliferation of a variety of risky lending practices during the first half of the 2000s.

To better highlight the effects of contemporaneous housing market and economic conditions on tenure choice, Exhibit 2 also shows homeownership rates of only those prime first-time home buying candidates who moved within the preceding year.[9] Like the data for all households, the data for recent movers show a substantial decline in the homeownership rate for prime first-time home buying candidates. In 2006, about three-quarters of recent movers were owner-occupants, but by 2012 the proportion had dropped to just over half. Declines for non-Hispanic white recent movers were similar to those for all recent movers.

What Might Be Behind the Homeownership Decline Among Prime First-Time Home Buying Candidates?

Mounting student loan debt has been discussed widely as a potential source of declining homeownership among young adults.[10] However, when the analysis of homeownership rates among young adults is restricted to householders who have a high school education or less, but who nonetheless have upper incomes and head nuclear families, the results are similar to those for college graduates (see Exhibit 3).[11] Between 2006 and 2012, the homeownership rate for prime first-time home buying candidates without college educations fell by 10 percentage points, and as of the latter year remained well below the rate recorded in 2000. Again, the trend was similar for the non-Hispanic white subgroup. These results suggest that rising student loan debts can't be blamed for the decline in homeownership among *all* prime candidates for first-time homeownership.

Exhibit 3. Student Loan Debt Doesn't Explain the Homeownership Decline Among Prime First-Time Home Buying Candidates Who Do Not Have College Educations

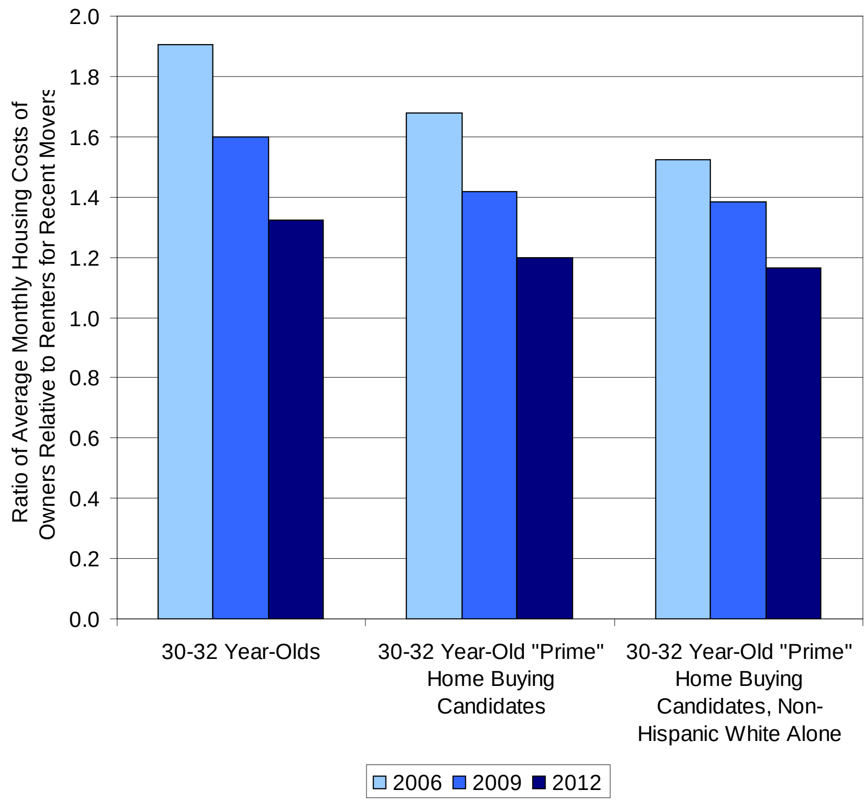


Source: U.S. Census Bureau, 2000 Census and American Community Survey Public Use Microdata Samples
Note: See footnote 11 for a discussion of changes between 2006 and 2009 in educational attainment classifications.

[9] Data are not included for 2000 because the 2000 Census did not contain a question on residence one year ago.
[10] For a discussion of the current debate surrounding the role of student loan debt in suppressing young homeownership, see Maia Woluchem and Taz George, "Is student debt hindering homeownership?" *Urban Institute MetroTrends Blog*, July 17, 2014, http://blog.metrotrends.org/2014/07/student-debt-hindering-homeownership/?utm_source=iContact&utm_medium=email&utm_campaign=Laurie%20HFPC&utm_content=July+2014+Newsletter.
[11] Caution should be exercised in interpreting the results presented in Exhibit 3. Beginning with the 2008 American Community Survey, respondents who received a high school diploma, GED, or equivalent degree also were asked if they had completed any college credit. Those who had completed college credit were removed from the high school graduates category and placed in the "Some college credit, but less than 1 year of college credit" or "1 or more years of college credit, no degree" categories.

The relative cost of owning versus renting is another factor that influences tenure choice. Although a full accounting of the costs of owning and renting is beyond the scope of this *Housing Insights*, an analysis of selected recurring housing costs for recent movers indicates that the cost of owning relative to renting declined substantially between 2006 and 2012 (see Exhibit 4).[12] Thus, homeownership rates declined for prime first-time homeowner candidates despite the fact that owning became more attractive relative to renting from a cost perspective.

Exhibit 4. The Cost of Owning Relative to Renting Declined Among Young Adult Recent Movers



Source: U.S. Census Bureau, American Community Survey Public Use Microdata Sample

Even if homeownership became more *affordable* relative to renting in the aftermath of the housing bust, it did not necessarily become more *accessible*. The reversal of loose lending standards in the aftermath of the housing bust likely contributed to the shift away from owner-occupancy among prime first-time home buying candidates between 2006 and 2012. During this period, the average FICO score of purchase mortgage originations rose, senior loan officers reported substantial credit tightening, and the Mortgage Bankers Association's Mortgage Credit Availability Index fell sharply.[13] In addition, a recent study by Goldman Sachs

[12] For renters, cost is measured by gross rent, which includes contract rent plus the estimated monthly cost of any utilities and fuels not covered by the contract rent. Units for which no rent is paid are excluded from the calculations. For owner-occupants, housing costs are measured by "selected monthly owner costs," which include payments for mortgages, deeds of trust, contracts to purchase, or similar debts on the property (including payments for first and subordinate loans); real estate taxes; fire, hazard, and flood insurance; utilities; fuels; and, if applicable, condominium fees. Costs for owner-occupied mobile homes also include, where applicable, installment loan payments, personal property taxes, site rent, registration fees, and license fees. The cost comparisons presented here do not reflect maintenance and improvement costs for homeowners, the tax benefits of homeownership, or the potential for wealth accumulation associated with homeownership, nor do they account for the opportunity costs associated with the larger up-front investment of ownership relative to renting. Differential shifts in the average size and quality of homes rented and owned by recent movers also might have affected these cost comparisons. In Exhibit 4, changes in the ratio of owner costs to renter costs for non-Hispanic whites were not statistically significant.

[13] According to CoreLogic data, the average FICO score on purchase money mortgage originations increased from 717 in 2006 to 740 in 2012. For other indicators of credit tightening, see Figure 2.1, Board of Governors of the Federal Reserve System, "Measures of Supply and Demand for Residential Mortgage Loans," *April 2014 Senior Loan Officer Opinion Survey on Bank Lending Practices*, May 5, 2014, and Mortgage Bankers Association, *Mortgage Credit Availability Index*, http://www.mbaa.org/ResearchandForecasts/MCAI.htm.

examined several dimensions of mortgage credit availability and concluded that, "lending standards remain squarely at the tight end of the historical distribution."[14]

A variety of other factors also might have influenced homeownership trends for prime first-time home buying candidates. Even among prime home buying candidates, credit scores and household savings might have declined during the Great Recession, thereby affecting the ability to qualify for a home purchase mortgage. In addition, although the analysis is limited to households who have upper incomes and should have good long-term earnings prospects due to their college educations, it does not account for the possibility that the economic downturn increased income volatility or created greater uncertainty regarding their future employment or income prospects. Indeed, consumer survey data indicate that expectations for future real income gains have declined and fear of future job loss has increased among young adults in recent years.[15] Previous research suggests that increased employment and income uncertainty has a detrimental effect on homeownership attainment.[16] And although the large majority of young renters still view homeownership as a better financial choice than renting[17], the severe house price declines of the housing bust could have altered young adults' assessments of future investment returns on homeownership. Finally, the foreclosure crisis increased the volume of tenure transitions from owning to renting.[18]

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[14] Hui Shan, "Are mortgage lending standards easing?" *The Mortgage Credit Analyst*, Goldman Sachs, July 11, 2014. The study examined seven different measures of mortgage credit availability: FICO score, loan-to-value ratio, mortgage spread, home sales financed with cash, percent of non-traditional loans, percent of loans not backed by the GSEs or the government, and responses to the Federal Reserve's Senior Loan Officer Opinion Survey. In assessing current conditions, the study assumed that the period between 2000 and 2002 represented a "normal" mortgage credit availability environment.

[15] The Thomson Reuters/University of Michigan Surveys of Consumers shows that among adults aged 18-34, the mean expected probability that real family income would be greater in 5 years declined from 53.9 percent in 2000 to 48.8 percent in 2006, and fell further to 45.7 percent in 2012. For the same age group, the mean expected probability of the respondent or spouse losing a job in the next five years increased from 20.4 percent in 2000 to 25.0 percent in 2006, and rose further to 28.5 percent in 2012. These changes were not tested for statistical significance. (Source: Thomson Reuters/University of Michigan, *Surveys of Consumers*, Time Series Data, http://www.sca.isr.umich.edu/data-archive/mine.php.)

[16] Haurin, Herbert, and Rosenthal summarize the research on income volatility and homeownership as follows: "Together, results from these studies suggest that job stability and income security are important predictors of the demand for homeownership. Such behavior on the part of households is rational because a household with an uncertain income stream and/or insecure employment is likely to be more risk averse. Because housing is a potentially risky asset, homeownership is less appealing for such households." See Donald R. Haurin, Christopher E. Herbert, and Stuart S. Rosenthal, 2007, "Homeownership Gaps Among Low-Income and Minority Households," *Cityscape* (9, 2): 12.

[17] Sarah Shahdad, "What Younger Renters Want and the Financial Constraints They See," *FM Commentary*, Fannie Mae, May 6, 2014.

[18] Molloy and Shan find that most individuals who experience a foreclosure and subsequently move end up renting. See Raven Molloy and Hui Shan, "The Post-Foreclosure Experience of U.S. Households," *Finance and Economics Discussion Series* (2011-32), Federal Reserve Board, May 2011.