High costs are eroding California's status as a competitive place in which to do business.

Affordable Housing and the California Economy

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In California on January 1 of this year, a median-priced home cost $192,000—a price that would typically require a downpayment of $38,500 and an income of $63,300 per year. The 1990 Census estimates the median household income in California to be $33,290.

Is it any wonder that last year (1990–1991), for the first time in its history, more 30-to-45-year-old Californians left the state than moved in? It is unlikely to be the last year in which California loses more of its productive younger workers than it attracts from the other 49 states. Who can blame the emigrants when single-family detached homes located in desirable neighborhoods can be purchased in so many other states for under $100,000.

Why should we be concerned about this? It is certainly a problem for the individuals involved and, on a personal level, we all hope and expect that affordable housing choices will be available for our children, our parents, and ourselves.

But it is also a societal problem. A region with high housing prices cannot compete economically. The continued lure of homeownership will pull many middle-income Americans to lower-cost living areas. Because jobs in the 1990s will continue to follow the labor base, living-cost differentials will reinforce previous regional shifts toward job growth in the Rustbelt, the Southwest, the Plains, and the Rocky Mountain states. A new emphasis on productivity and cost-competitiveness is already propelling mid-sized and larger companies to move or expand their facilities into locations with lower costs of living.

A recent analysis conducted by Gruen Gruen + Associates found a perfect, or 100 percent, correlation between the relative change in cost of living in states and changes in state employment. Based on the change in nonagriculture payroll employment in the recessionary period from November 1990 to November 1991, and the change in the relative cost of living index from 1980 to 1990, the eight states that were the top job losers in either percentage or in absolute terms had higher relative costs of living in 1990 than in 1980. Conversely, the relative cost of living dropped between 1980 and 1990 in all four of the states that had the highest job increase. California, with 135,300 jobs lost, was on the losers' list. Among the winners, states with the most significant absolute gains in employment were Texas, Arkansas, Nebraska, Colorado, and Utah.

In California, the price of houses has escalated faster than incomes. One cause has been strong demand. As the baby boomers have matured and large numbers of immigrants have arrived, competition for affordable ownership housing has put pressure on home prices. This is particularly true where housing production has been restricted.

In fact, growth and demand for housing have led to restrictions on housing development in many areas. Residents' concerns about crowding, their interest in maintaining their property values, their preference for separation of land uses, and, let's face it, their desire to exclude certain categories of lower-income people, have led to enactment of various kinds of growth controls.

Growth controls restrict the production of new housing and thereby drive up prices. In addition, in recent years, local governments have adopted many other well-intentioned regulations designed to carry out such goals as environmental protection, provision of adequate transportation facilities, and so forth. These regulations often entail fees and other requirements that raise the cost of housing.

If housing affordability is indeed a priority concern, all levels of government must recognize and understand the trade-offs involved. They need to be aware of how proposed regulations will affect housing affordability before those regulations are approved. Communities should monitor the ways in which their regulations affect housing affordability in order to alter those policies with particularly pernicious impacts.

The ULI Low- and Moderate-Income Housing Task Force commissioned a study by Ira S. Lowry and Bruce W. Ferguson aimed at analyzing the effects of development regulation on housing affordability. The researchers looked at how three different types of development regulations affected the price of land and housing in three metropolitan areas. The idea was to look beyond individual jurisdictions to the overall impact of regulations in all jurisdictions within a regional housing market. The

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three housing markets singled out—Sacramento, Orlando, and Nashville—operated under the dictates of different regulatory styles. The researchers interviewed local planning officials and residential developers in numerous jurisdictions in the three metropolitan regions. The purpose of this effort was threefold:

- to measure the incidence of various kinds of development regulation;
- to find out how regulations were viewed by the regulators and the regulated; and
- to learn how land and housing prices and production in each housing market had responded to demand.

All three housing markets had recently experienced rapid population growth and residential development that strained the capacity of their infrastructure and public service systems, raising issues of growth management, public finance, and environmental protection. Yet the regulatory response in each metropolitan area was different:

- In California, state law requires local governments to review the environmental consequences of all proposed developments and to accommodate a "fair share" of population growth. Acting independently, cities and counties in the Sacramento area have devised powerful instruments to limit, channel, and exact fees from residential development in their jurisdictions.
- Tennessee is more laissez-faire. The state government has sought no role in development regulation and only a few local jurisdictions in the Nashville area have gone beyond traditional subdivision and zoning ordinances. But neighborhood organizations have become increasingly influential in deciding the fate of specific projects.
- Florida's state government has created an elaborate system of integrated regional plans and development reviews. The Orlando area generally has favored growth and neighborhood organizations have not influenced project reviews.

During the 1980s, reports the study, housing became more easily affordable in Orlando and Nashville, but far less easily affordable in Sacramento. Demand for housing was strong in both Sacramento and Orlando. Sacramento's stringent regulations limited housing production so that excess demand caused house prices to rise sharply after 1985. In contrast, Orlando's builders were able to keep pace with an extraordinary rate of population growth; as a result, price increases in Orlando were moderate throughout the decade.

This path-breaking study, published by ULI this year under the title *Development Regulation and Housing Affordability*, evaluates how housing prices in the three areas were affected by three types of development regulations:

- limits on development rights;
- impact and linkage fees; and
- procedural complexity and delay in issuing permits.

All three types of regulation were strikingly evident in the Sacramento housing market. Because of extensive development restrictions, only about 40,000 acres of land within 20 miles of the central city were both vacant and legally developable at the time of the survey. In two years, between 1988 and 1990, raw land prices in Sacramento County more than doubled, rising from $17,500 to $42,500 per acre. The typical impact fee was about $7,700 for a single-family house, and developers estimated the value of entitlements at $85,000 per acre. All told, development regulation added about $26,000 to the cost of a typical new house—about one-fifth of the 1989 median new home sales price of $131,000.

Remarkably, few planners in Sacramento localities thought that their jurisdictions' regulations affected the pace, price, or location of residential development. But perhaps this is not so remarkable, because Sacramento planners typically compare their regulatory policies with those of other California jurisdictions.

Unfortunately for California's economy, Sacramento is not just competing with the Bay Area and other valley communities, but with Phoenix, Colorado Springs, and a host of many other lower-cost communities within the United States. In general, the regulators in the Sacramento region felt that market forces would counteract the effects of regulations. The study clearly shows that this was not, in fact, the case. Regulation was the key factor causing housing prices to rise. In 1990, the cost of securing development rights for a house in Sacramento was twice the cost of raw land for it.

As long as fiscal planning and jurisdictional mercantilism continue in the ascendancy, California will be unable to deal with the primary economic challenges facing the state. These challenges include the shift in spending from defense to nondefense industries, the imbalance between the type of high-value-added jobs that are needed and the skill level of the labor base, the significant water shortage and competitive pressures facing the agriculture industry, and the growing social and economic imbalances in center cities. It is none too soon not only to seek better ways for leveraging California's still substantial resources to provide subsidized housing, but also to seek ways to encourage housing developers to overbuild. An overbuilt housing market could make California a competitive place in which to do business and a state that young productive workers will, once again, want to move to, not from. ❖

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