

TOMORROW'S HOUSING: THE FUTURE OF CALIFORNIA REAL ESTATE

EXECUTIVE REPORT



THOUGHT LEADERSHIP
EXPO PANEL 2013

CALIFORNIA ASSOCIATION OF REALTORS®

PREFACE



Joel Kotkin

Joe Mathews

Perry Wong

Joel Singer

This executive report presents analysis from a panel convened by the CALIFORNIA ASSOCIATION OF REALTORS® in October 2013 at its annual EXPO conference. CEO Joel Singer moderated the panel for an engaging discussion on how future housing markets and public policy can reflect the needs and desires of Californians, and why addressing concerns about affordability and upward mobility will keep the American Dream of homeownership attainable.

This panel was part of C.A.R.'s new Thought Leadership initiative, and among its characteristics are high-level events that place an emphasis on intellectual engagement. A focal point of the Thought Leadership program is to pursue dialogue that adds clarity to the challenges and opportunities that will shape the future of housing.

PARTICIPANTS

Joel Kotkin

Author and journalist

An internationally-recognized authority on global, economic, political, and social trends, Joel Kotkin is the author of *The Next Hundred Million: America in 2050*, published by Penguin Press. The book explores how the nation will evolve in the next four decades. He is also the author of the critically acclaimed book *The City: A Global History*.

Kotkin is the Roger Hobbs Distinguished Fellow in Urban Studies at Chapman University and Executive Editor of the widely read website www.newgeography.com. He writes the weekly “New Geographer” column for Forbes.com. He is a Senior Visiting Fellow at the Civil Service College in Singapore. He also serves on the editorial board of the Orange County Register, writes a weekly column for that paper, and is a regular contributor to the *Daily Beast*.

Joe Mathews

Author and journalist

Joe Mathews is California editor for Zócalo Public Square, a Los Angeles-based ideas exchange that combines daily humanities journalism and live events, and writes the syndicated Connecting California column for Zócalo and 20 publications around California.

Mathews also serves as a fellow with Arizona State University’s Center for Social Cohesion, and co-president of the Global Forum on Modern Direct Democracy—which brings together academics, journalists, activists, and other experts on initiative, referenda, and new forms of deliberative and participatory democracy. He is co-author, with Mark Paul, of *California Crackup: How Reform Broke the Golden State and How We Can Fix It* (University of California Press, 2010).

Formerly a reporter at the *Los Angeles Times*, *Wall Street Journal*, and *Baltimore Sun*, Mathews also serves as senior fellow at the New America Foundation, as a contributing writer at the *Los Angeles Times*, as a blogger at Fox & Hounds Daily, and as radio and TV commentator on all things California.

Perry Wong

Director of Research
Milken Institute

Perry Wong is Director of Research at the Milken Institute. Wong is an expert on regional economics, development and econometric forecasting, and he specializes in analyzing the structure, industry mix, development, and public policies of a regional economy. He designs, manages, and performs research on labor and workforce issues, the relationship between technology and economic development, and trade and industry, with a focus on policy development and implementation of economic policy in both leading and disadvantaged regions. Wong is actively involved in projects aimed at increasing access to technology and regional economic development in California and the American Midwest. His work extends to the international arena, where he is involved in regional economic development in southern China, Taiwan, and other parts of Asia.

Wong has conducted many research studies regarding regional economic development and policy impacts on both public and private fronts. These include the impact of U.S. budget and trade policy changes on key U.S. industries and regions.

Joel Singer

Chief Executive Officer
CALIFORNIA ASSOCIATION OF REALTORS®

Joel Singer is Chief Executive Officer of the CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.), a statewide trade organization with 160,000 members dedicated to the advancement of professionalism in real estate. He also is President and Chief Executive Officer of zipLogix™, whose software is used by more than 600,000 REALTORS® in 48 states.

Singer has held the Association’s top staff position since November 1989. He previously served as C.A.R.’s Chief Economist and headed the Association’s Public Affairs Department. He also has been directly involved in the development of key business technologies and significant housing legislation in California.

Before joining C.A.R., Singer spent several years as a Chancellor’s Intern Fellow at UCLA and a Fulbright Fellow in West Germany.

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The CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.) is a statewide trade association dedicated to the advancement of professionalism in real estate. C.A.R. celebrated its centennial anniversary in 2005. The Association works in conjunction with 120 local associations of REALTORS® throughout the state, as well as with the NATIONAL ASSOCIATION OF REALTORS®. Serving nearly 160,000 members statewide, C.A.R. provides a wide array of products and services to meet diverse member needs. Additional background on C.A.R. and its services can be found at car.org

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Part I

Job Growth and Housing Affordability

Inevitable demographic, economic, and environmental changes will prompt housing to evolve, but the overarching question on the minds of panelists was whether policy will facilitate or hinder conditions favorable to homeownership — especially if affordability and upward mobility remain lingering concerns in California. In the aftermath of the systemic failures made plain by the financial crisis, the panelists' outlook on the future of real estate was informed by the immediate trend of sluggish employment, as well as the broader and longer-running trend of soaring inequality. Consequently, chief among the points emphasized during the panel discussion was the importance of jobs – principally working and middle class jobs – to the long-term viability of housing. Perry Wong commented, “We really have to build a job base. Everything is about jobs, including housing. It’s not actually about housing.”

However, while the economy is slowly recovering from the Great Recession, the labor market has seen a decline of seven percent in the employment-to-population ratio, whereas corporate profits are up 42 percent, and financial profits have increased by nearly 60 percent. Also, according to recent figures from the Social Security Administration, the median wage in 2012 was at its lowest level since 1998, which means that at least half of the workforce is getting left behind as top earners and corporate profits continue to gain. And as home prices rise again five years after the crisis, affordability drops as values increase and incomes stagnate.

Amidst such economic disparity, a topic as broad as the "Future of California Real Estate" has no shortage of relevant angles to discuss, but in examining tomorrow's housing, C.A.R. CEO Joel Singer began by leading panelists to think about affordability in the context of the peaks and valleys that California prices have experienced over the past few decades. Singer added that historically, California housing prices have been above the national average, so while it can be difficult to afford to buy, he remarked that at the same time "you can't afford **not** to buy in California."



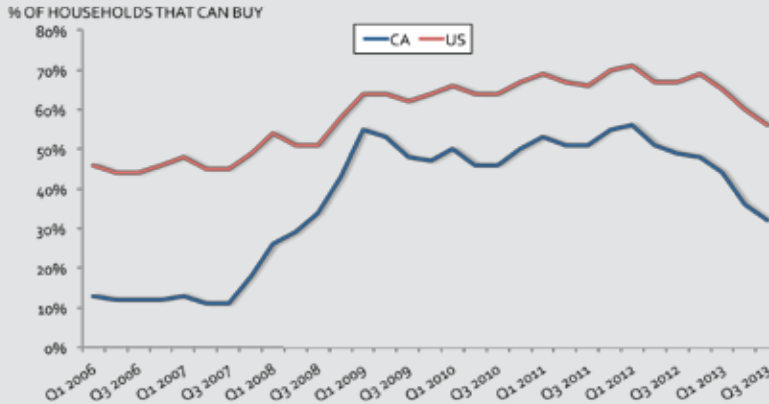
Singer noted that after the collapse of the housing market, it was broadly forecast that housing affordability in California would increase, and such prices would create opportunities for first-time buyers. However, while housing affordability did approach the national average, it has since contracted and Singer stated the following: "An opportunity for first-time buyers has been squandered, and it's visible in the marketplace. It's visible because at this point in time, normally in the housing cycle about 50 percent of your buyers will be first-time buyers. We're still mired by the number of all-cash buyers, the number of investors in place, and the number of people coming with capital from overseas, so the first-time buyer number is really far lower than it should be. The self-correction that we always assume is going to come

hasn't come."

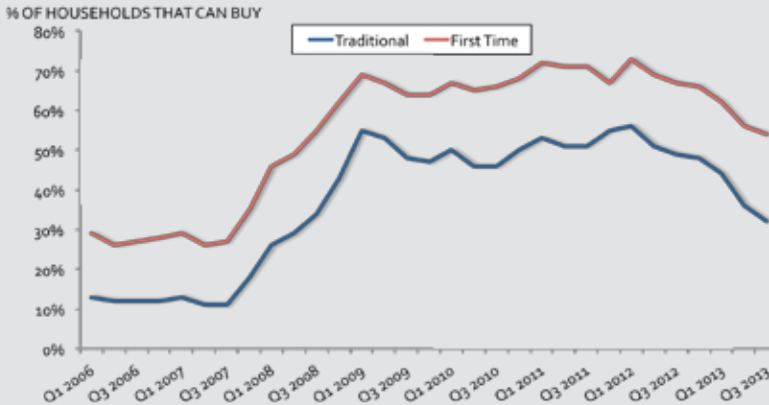
Singer's points are reflected in research from C.A.R., as its Traditional Housing Affordability Index (HAI) indicates that for the third quarter of 2013, the percentage of home buyers who could afford to purchase a median-priced, existing single-family home in California dropped to 32 percent, which is far lower than the index rating of 56 percent for the overall nation. Housing affordability fell for the sixth consecutive quarter in the state, and reached below 35 percent for the first time since the third quarter of 2008. C.A.R.'s First-time Buyer Housing Affordability Index for a single-family, entry-level home in the second quarter of 2013 was 56 percent, which falls far short of an index rating of 75 percent for the country as a whole.

Housing Affordability Index

• California vs. U.S.



• Traditional Home Buyers v First Time Buyers



Source: CALIFORNIA ASSOCIATION OF REALTORS®

“As the wealthy in California, particularly in the Silicon Valley, are having the best of times, for most of California’s middle and working class, it’s not so great. And I think long-term that affects the [housing] market.” — JOEL KOTKIN

Wong reiterated that addressing affordability links back to strong job opportunities in order

to facilitate favorable circumstances for housing, and as a result, the long-term implications of first-time

buyers being constrained to the sidelines are problematic at a time when the housing recovery remains fragile. In light of these challenges, he posited that we need to ask ourselves whether the nation’s financing model can create an environment that enables the housing market to perform optimally, so that not only current housing needs are addressed but also the needs of future markets. As an example, Wong pointed to the economic struggles of Millennials and stated the following:

“If you look at today’s market for a [young person], even if they have decent monthly income, how many of them can pay down 20 percent? None. Not many. So in that sense it is policy not enabling a market to perform [as it should]. Meaning that we have a lot of quality buyers out there, but they don’t have a 20 percent down payment. So someone has to address an issue of access to money in a way that is sound — a system that can be resilient, even in an economic downturn. And so the government cannot be the agent to say, ‘I am the ruler, so you must follow this hard line requirement.’ [We need] government that can guarantee safety while letting private capital do its work.”

Kotkin expanded Wong’s points by noting that affordability issues after the downturn have affected not only younger Americans but also minorities, particularly Latinos and African Americans and their ability to become homeowners. He expressed concerns about class- and skills-based bifurcation, as it is not in the interests of a robust housing market if the state only has isolated high-growth regions as opposed to widespread job growth to develop California’s middle and working classes. Kotkin added that the state is already experiencing symptoms of these conditions, stating, “As the wealthy in California, particularly in the Silicon Valley, are having the best of times, for most of California’s middle and working class, it’s not so great. And I think long-term, that affects the [housing] market.”

Perhaps a sign of these long-term effects is a recent study showing the trend in income segregation in American neighborhoods, which establishes that socioeconomic residential sorting has grown substantially in the last 40 years. The report states, “In 1970, 65 percent of families lived in middle-income neighborhoods (neighborhoods in one of the two middle categories);

“We’ve become a homegrown state. [...] We’re much more dependent on ourselves. We need people, and we need growth, and we need it yesterday.”

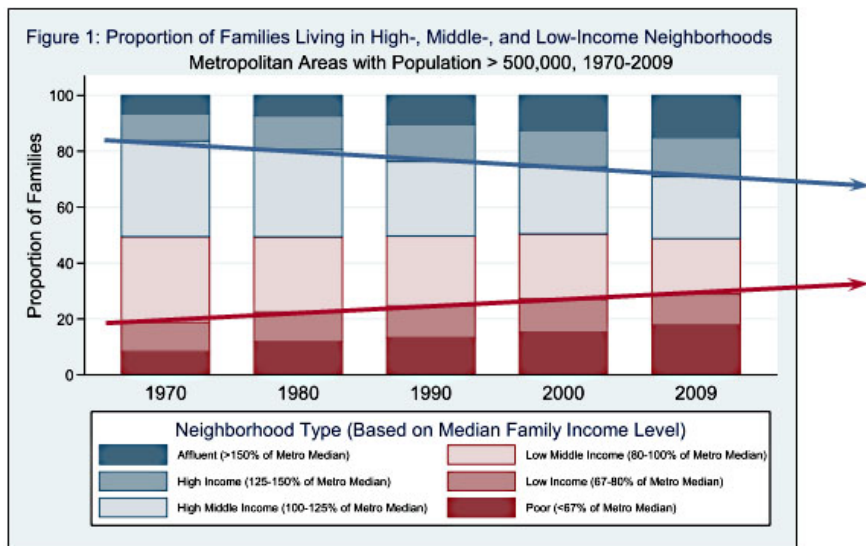
— JOE MATHEWS

by 2009, only 42 percent of families lived in such neighborhoods. The proportion of families living in affluent neighborhoods more than doubled from seven percent in 1970 to 15 percent in 2009. Likewise, the proportion of families in poor neighborhoods doubled from eight percent to 18 percent over the same period. Thus, in 1970 only 15 percent of families lived in one of the two extreme types of neighborhoods; by 2009, that number had more than doubled to 33 percent of families.”

In terms of how this trend is evident in pricing, Kotkin

stated the following: “We used to be ground zero for the American Dream. Housing prices in California had a median multiple. A median multiple is the ratio of housing, median housing price and median household income. I think it really is the most relevant measurement. And we were always the same. Even if San Francisco people were making 50 percent more, housing was 50 percent more. That is totally out of whack, and by 2013, the price differential was about 113 percent. By the way, rents follow that, as well.”

To contextualize the state’s affordability issues with a



Source: Kendra Bischoff, Cornell University; Sean Reardon, Stanford University

“big picture” outlook, Wong stated that what will matter in the years to come is whether as a region and a country we’re able to change when we see significant problems arise because housing will require a vibrant economy that can create not just income but more importantly, wealth. Ultimately, the panelists warned that if wealth is concentrated in the hands of the few and the American middle class suffers, severe bifurcation reduces the living conditions of the poor to a mere abstraction due to reduced interaction and shared experiences.

As a solution, much like Wong, Kotkin stressed job growth, stating, “We just have to figure out how we restart the middle- and working-class job engine in California. Everything else is secondary in my mind.”

However, even if job growth and affordability improve in the state, both Wong and Singer were keen to point out that the lucrative nature of home prices in parts of the state is entirely justified in light of the overall attractiveness of California as a desirable place to live due to its weather, cultural magnetism, booming technology industry, and global stature — all of which will naturally be reflected in real estate prices.



While agreeing that the state has many advantages, Joe Mathews still cautioned that California cannot afford to rest on its laurels as a diverse and global center of trade because its stature as a state of arrival has diminished and, in his words, “We’ve become a homegrown state. [...] We’re much more dependent on our-

selves.” He added, “We need people, and we need growth, and we need it yesterday.” But the growth and affordability emphasized by the panelists are impacted by the state’s opportunities for upward mobility, which was discussed as an equally important factor to the future of real estate in California. ■

Part II

Upward Mobility and Future Homeownership

Upward mobility is far from tangential to the issues of affordability and job growth, so Singer also led panelists to consider the tenability of opportunities for advancement and the consequences for the housing market if working and middle class Californians cannot aspire to homeownership. In Kotkin's estimation, one of the fundamental questions facing California is upward mobility. A demographic component is central to this question, as without advancement, household formation will be affected as people choose to have fewer or no children on account of sheer unaffordability.

Kotkin stated, “The problem is when upward mobility begins to become harder and harder to achieve, it has ramifications that affect the economy, I think as we saw in Japan. And it has ramifications in terms of family formation. The family is the basis of the society, but it’s becoming more and more difficult.”

He pointed out that California’s number of children is dropping, whereas the number of children in other states is rising since it is more affordable elsewhere. Kotkin also noted that Los Angeles is a prime example of this cause and effect, as research indicates the foreign-born are older than the native-born because children of immigrants have left due to a lack of upward mobility.

Singer added that demography is destiny and questioned what will happen to in-migration in the state, especially if upward mobility is seen as lacking. Singer queried, “Are we losing our edge internationally? Or are we actually increasing our edge internationally?”

Mathews simply posited: “We’re not in the 1980s anymore. We had record levels of immigration. The immigrants are not coming. And we’re not having children. We’re just not having children.” Thus, real estate and household

formation in California could be shaped by a divide between those who can afford to have children and house them comfortably versus those with limited upward mobility.

As to whether the divide in upward mobility is primarily on the basis of race or educational attainment, panelists slightly differed but emphasis was greatly placed upon the significance of education to developing a workforce capable of pursuing homeownership. According to Mathews, a key reason that California has lost its edge boils down to education. He stated, “The real secret sauce of the state was cheap – free in many cases – high-quality public higher education. In 1912, Berkeley was already the largest public university in the world, and we’ve essentially lost our advantage. This state saw a decline by six points in the percentage of its population that has college degrees in the last decade. That is death.”

Mathews went on to connect his personal story of place as a Californian to ideas about upward mobility in the state by describing the progression in quality and affordability in the types of houses his grandparents, parents, and he himself could all afford to buy over the past few decades — with each transaction shrinking in attainability. A key takeaway from his personal narrative was the role that the generational transfer of wealth played in the pursuit of home-buying during his family history. He posited that we’re about to see the greatest private generational transfer of wealth in the history of the world, and REALTORS® will be intimately involved with that transfer.

But Mathews warned, “The question is how – as a state – do we use that transfer in ways that give us a greater future? The bad news, and this is where my story comes abruptly to a close, is that there’s no earthly chance of us getting

“The problem is when upward mobility begins to become harder and harder to achieve, it has ramifications that affect the economy, I think as we saw in Japan. And it has ramifications in terms of family formation”

— JOEL KOTKIN

that right. We're not even talking about it. And more profoundly, and this is the focus of my journalistic work about California, our governance system – and I use the word 'system' charitably in California – is not up to the task of making those kinds of forward-looking decisions." Mathews added that these transfers of wealth may serve to preserve and enhance inequities if the attainability of homeownership is increasingly tied to familial wealth.

Kotkin agreed that intergenerational transfers will influence housing, but he pointed out that increasing health care costs along with greater longevity will affect these transfers of wealth and by extension, upward mobility, stating, "[Transfers] are going to come much later, much slower, and maybe a lot less money in it as people live longer and longer and longer." If that is the case, the housing market in California could feel the impact of home-buying patterns shaped by later transfers of wealth.

Ultimately, the underlying issue to the panelists' discussion on both affordability and upward mobility is public policy, and Singer observed that each panelist could agree on its importance to keeping the American Dream of homeownership feasible for all socioeconomic classes. ■



Part III

Public Policy

The dynamism of a state like California can stand in stark contrast to public policy that is constrained by the state's unwieldy scope, not to mention the difficulty of governing a polity with a mix of disparate regional economies defined by their own industries. When taking into account the political mobilization necessary to build job opportunities and income potential for middle- and working-class Californians, panelists expressed a mix of short-term pessimism and long-term optimism for the future of housing in the Golden State. Singer acknowledged that California faces significant policy problems, but drew the conversation to items of practical value and an enhanced understanding of what ails the state in order to focus the discussion on tangible courses of action.

Kotkin began by criticizing policies that inhibit growth, commenting, “When you see this dichotomy in the state, we have economic policies in California that make it very difficult for middle- and working-class people in the interior to ever make a decent income. [...] I did a report on the Inland Empire for Brookings several years ago when incomes were growing. We had expansion—warehousing, manufacturing, construction, all kinds of good-paying blue-collar jobs. But the policies of the state of California are absolutely designed to make those jobs very, very hard to grow. And if we don’t change that, nothing really can be improved.”

He added that California should primarily focus on reforming its regulatory environment, encouraging people to work from home by telecommuting, reducing fees, and addressing the high land costs throughout the state where applicable.

“It’s not a surprise to me that families are very resilient as long as we have a policy, a solution to facilitate it. So that’s how I look at the market as optimistic.” — PERRY WONG

Mathews emphasized the importance of public policy centered on investing in the future, particularly education and infrastructure. He said, “We are deeply locked into a narrative at the state level of austerity. [...] But people are afraid to invest more because they don’t think more money coming to the state is going to end up in education and infrastructure where it’s so desperately needed, where we’ve underinvested. It’s going to be gobbled up by public employees and other interests. And we need to grow. We need to get into the mode of spending money to make money, which is how this state grew.”

He also pointed to Singapore as an example of a country utilizing policy oriented around the future, specifically incentivizing savings, which ultimately benefits the housing industry. Singapore provides several thousand dollars in a savings account for the birth of a child. Mathews stated, “That’s the kind of society that is at least thinking about the future and making choices.”

Speaking of savings and families, Wong noted that he sees room for optimism because families, particularly immigrant families, are finding ways to make homeownership attainable by pooling resources, and as a result, policy should assist, not hinder, this reality. He stated, “It’s not a surprise to me that families are very resilient as long as we have a policy, a solution to facilitate it. So that’s how I look at the market as optimistic.”

Perhaps another reason for optimism is the panelists’ discussion on the ways in which California’s regionalization can be an advantage in spearheading policies. Wong stated, “Regions are capable of repairing [and] regenerating — that actually is key.” He added, “If we can think of a balanced way to allow some regions to be creative in finding their own way to build a job base, [then] I think that is the only solution I can see.”

Wong pointed out that companies from the coastal regions need to be prevented from moving out of state, and in order to retain those companies within California, policy should encourage them to move inland into regions that need jobs the most, such as the Inland Empire and the Central Valley.

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Without improvements in some regions, Kotkin stated, “I think you’re going to see a lot of struggle in many areas.” In acknowledging the central role of public policy in shaping the future, he restated, “Again, I think if we keep on the path we’re on, it’s pretty clear where we’re going to end up, which is increased bifurcation.”

Policies that keep real estate accessible and allow California to put its own unique spin on the American Dream of homeownership won’t come overnight, according to the consensus of panelists, but they noted that a strong housing market remains an essential piece of the puzzle for the Golden State’s future; after all,

each panelist chooses to reside and remain in California for a reason, which is perhaps a sign that they ultimately fall on the side of optimism, despite the variety of challenges addressed during the panel. ■



Part IV

Concluding Remarks

Singer concluded the panel with a few comments on the major themes and lessons of the viewpoints shared by the discussants, such as the future is not a given when it comes to real estate, and that public policy and facts really matter in shaping the future lives of everyday Californians and where they call home. Singer stressed that being able to anticipate what's important is the first step toward action, but it's necessary to understand that the dynamics of the market/real estate are not always explicable to begin with. He stated, "Given everything that we've heard, most of which I agree with, it's still hard to imagine the recovery we just experienced. It may be very transitory, or it may be another bubble. I don't think so, but it may be. There's something else going on here. [...] And so as we look at these problems, my request to all of you is that we engage in this rationally."

To Singer's point, engaging in substantive discussions through rational discourse is a central tenet of C.A.R.'s Thought Leadership program in order to add clarity to the most pressing issues that will shape housing now and in the years to come. ■

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