MILLENNIALS AND HOMEOWNERSHIP

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and Elliot Schreur

For young people throughout the twentieth century, and down to Millennials today, becoming a first-time homeowner has represented a symbolic milestone along the road to adulthood. From a financial perspective, owning a home can be a rewarding investment, providing a means to take advantage of generous tax breaks and accrued equity. Buying a home also allows families to access neighborhood amenities and a range of intangible benefits that come with residential stability. While homeownership is not always the right choice—financial or otherwise—for families in all circumstances, it has historically been one of the most desired and valuable assets on the balance sheets of American families. Yet the Great Recession may have changed the calculation young families make when thinking about becoming a homeowner.

Current Conditions

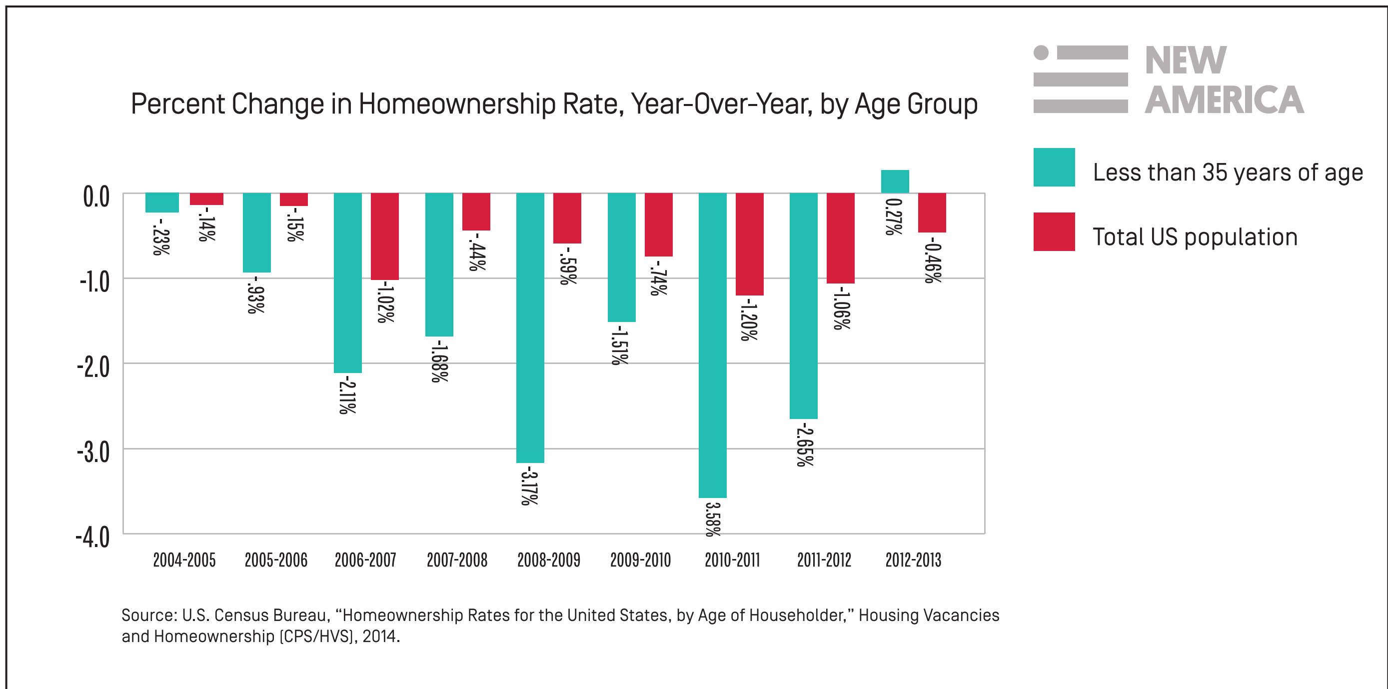
Homeownership in America peaked at over 69 percent in 2004-2006, when lax oversight and irresponsible credit contributed to the inflation of a housing bubble. Along with housing prices, the ownership rate for all age groups soared, including for Millennials who were just entering the household-forming stage of life.[1] Millennials entered the housing market at record levels for their age group: The percentage of Americans under age 25 who owned a home surpassed 25 percent for the first time in 2004, up from just 14.8 percent in 1993.[2] Similar gains were seen for the age group between 25 and 29, 41 percent of whom were homeowners in 2005.[3]

The bursting of the housing bubble ushered in a new reality for families aspiring to own a home. Housing prices dramatically declined, defaults and foreclosures went up, and mortgage credit tightened. By 2013, after the worst of the recession had past, young Americans had experienced the largest declines in homeownership compared to the peak years of 2004-2006.[4] Although the subset of "young families" corresponding to later Gen Xers (born 1969-1978) experienced the greatest decline of any age group during the recession, Millennials (born after about 1980) fared almost as badly. The homeownership rate for Millennials aged 25-29 has bottomed out at 34 percent, near the lowest rate on record.[5] For all ten-year age groups between 25 and 54, the homeownership rate is at its lowest point since record keeping began in 1976.[6]

The rate for young adults (aged 18 to 34) has fluctuated widely over the last 30 years, falling to around 33 percent in the early 1990s and reaching above 41 percent in the mid-2000s.[7] The current rates of homeownership among Millennials aged 30-34 are 2 percentage points below those at the same age in 1993.[8] While there is no objective baseline that sets the optimal homeownership rate for young people, regardless of what the homeownership rate "should" be, the fact remains that since Millennials have come of age they have experienced a convulsing housing finance system and a housing market in which incidence of homeownership has consistently declined.

In response to the recession, lenders have tightened mortgage standards and are requiring more money down to finance loans. Between 2007 and 2013, the median down payment for the cheapest 25 percent of homes (meaning those most likely to be sought by first-time homebuyers) increased from $6,037 to $9,480, an increase of 57 percent in just six years.[9] Granted, this is comparing today's average down payment to that during the lead-up to the housing-finance crash when standards were most lax, but the pattern holds for longer time spans as well. The down payment for the cheapest 25 percent of homes was 7.5 percent of the sales price in 2013, compared to an average of just 4.2 percent for the period between 2001 and 2007.[10]

Millennials' disappointing experience with the housing market has naturally shaped their attitudes about homeownership. Most Millennials believe that owning a home may not offer the kinds of financial benefits it once did. A large majority (62 percent) believes that it is less likely for families to build equity and wealth through homeownership than it was 20 or 30 years ago,[11] and two-thirds of Millennials (compared to only half of people over age 65) think renters can be as successful as homeowners.[12]



Even though Millennials have experienced firsthand some of the risks involved in homeownership, such as foreclosures and severe price drops, they still largely view owning a home as a lifetime goal. According to a 2014 Fannie Mae survey, about three-fourths of Millennial renters and nine out of ten current Millennial homeowners think that owning a home is a better choice than renting.[13] The Federal Reserve Board found that general concerns about the current financial viability of homeownership, rather than preferential prejudices against the idea of homeownership, was the most common response Millennials gave for renting as opposed to owning a home.[14] Half of respondents under age 30 reported that not being able to afford the down payment for a home was the top reason for not owning a home.[15] These results suggest that the primary obstacles to higher homeownership rates for Millennials are related to the current financial status of Millennials.

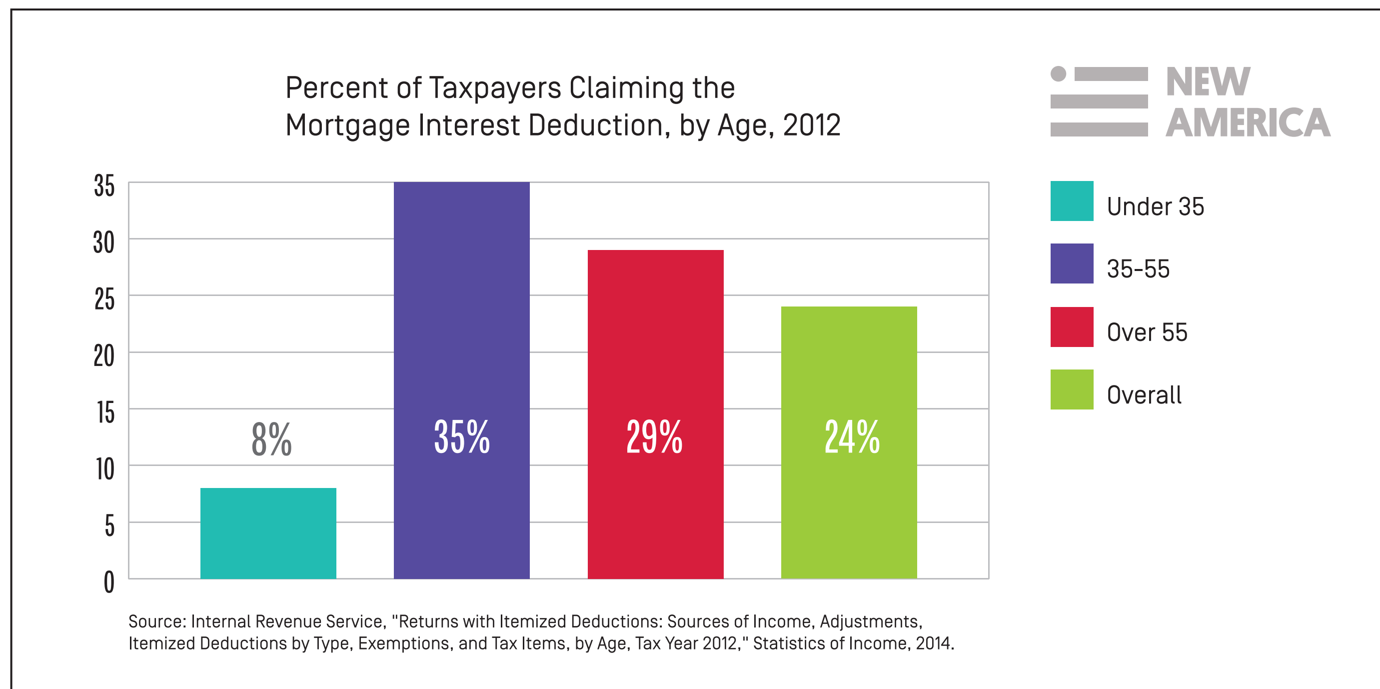
Other factors that are lowering the incidence of homeownership among Millennials may be related to emerging attitudes and preferences. Changing demographic trends, such as declining marriage and child rearing, reflect life style choices that may move some young adults away from homeownership.[16] Millennials may seek to live in greater proximity to other urban resources, making suburban developments less attractive. They may opt to live longer with friends or family than choose to live alone. In short, there may be particular characteristics of today's young people that reflect a more idiosyncratic relationship with homeownership than previous generations had.

Even if the Millennial generation catches up to the homeownership rate of previous generations, it will happen at a later age, meaning that the generation may have a harder time building up home equity and taking full advantage of the financial and social benefits of homeownership over the life course.

Policy Landscape

The ability to become a homeowner in the United States is dependent on a number of factors, including having the ability to make a downpayment, qualifying for a mortgage, finding a house that is affordable, and being able to consistently make loan payments from income over the long term. All of these elements must come into alignment for a family to be able to responsibly purchase and maintain ownership of a home. But since the recession, each of these factors has become more challenging, and few of the current policy supports in place to support homeownership are well positioned to help younger households.

For example, the mortgage interest deduction, one of the single largest tax expenditures, costs taxpayers about $74 billion a year,[17] yet it largely fails to achieve its purported purpose of helping Americans afford homes.[18] First of all, it provides benefits only after people have already become homeowners, rather than helping them prepare for their first purchase. Second, this tax provision rewards those with higher mortgages and misses homeowners who take the standard deduction on their income tax and do not itemize their tax deductions. Only about 31 percent of taxpayers



itemized their tax deductions in 2012.[19] The vast majority of the benefit of the mortgage interest deduction

goes to the highest-income households, who are most likely to purchase homes even in the absence of the mortgage interest deduction. According to the Center on Budget and Policy Priorities, "77 percent of the benefits from the mortgage interest deduction [go] to homeowners with incomes above $100,000, almost none of whom face severe housing cost burdens."[20] Millennials as a group are increasingly likely to have low incomes, which puts them at a distinct generational disadvantage in profiting from this regressive tax expenditure.[21]

Other policy efforts miss the mark because they are intended to assist current homeowners rather than help families achieve homeownership for the first time. In response to the rising rate of foreclosure, the government backed the refinancing of distressed loans. This policy approach, which was implemented by the Obama Administration, was largely ineffective at promoting homeownership for the youngest and most recent homeowners. These owners had low levels of equity built up in their homes when prices fell, and thus were the least likely to be able to refinance through this method.[22]

One defining feature of the U.S. housing market has been the widespread availability of mortgage financing. This was a primary force behind rising rates of ownership in the second half of the twentieth century, but it also played a role in creating the conditions that precipitated the Great Recession. Policymakers have not addressed the most basic questions of what the housing finance system will look like in the decades ahead. The government-sponsored enterprises responsible for providing housing financing, Fannie Mae and Freddie Mac, remain in government receivership. There appears broad consensus that this is unsustainable, but Congress has yet to take action on establishing a new set of rules.

The Challenges to Address

The slowdown of home buying among young Americans is potentially troubling for several reasons. First, pursuing homeownership early is a key factor in being able to build wealth over the life course.[23] Homes are often the largest item on a family's balance sheet.[24] If other avenues to building wealth and assets are not opened instead, the current, lower trajectory of homeownership among Millennials may remain a drag on the generation's finances over their lifetime. Second, homeownership has been a way that families access valuable services. It is the residential stability, in addition to the fact of ownership, that may bring additional benefits. Third, homeownership appears to be an enduring aspiration of many young families, who see it as a primary marker of achievement in and of itself.[25] While ownership is not appropriate for many people given the risks and responsibilities, there should be viable pathways available for those that pursue this experience.

Given the prevailing uncertainty in the housing finance system, it remains to be seen if public policy can be crafted

to help young families become homeowners in sustainable and responsible ways. Lending standards have tightened in response to the bursting of the housing bubble that brought on the Great Recession. However, policymakers have yet to act on large-scale reforms to fix the housing finance system. Policymakers will need to balance the objectives of making sure mortgage credit is available to worthy borrowers and setting new standards to protect consumers in the financial services marketplace. Regulatory oversight of financial services is needed to ensure high-quality mortgages are offered with appropriate underwriting standards. Eliminating the availability of predatory financial products will go a long way to mitigating the high levels of risk that become apparent during the recent housing crisis.

Another challenge to address is ensuring that there is sufficient supply of affordable homes accessible to first-time buyers with modest resources. In some cases, it may require expanding the models of housing ownership, to include cooperatives and shared equity projects. These arrangements, along with protections for renters, can offer some of the benefits of ownership while also expanding choices in tenure in ways that might match the preferences of a larger number of Millennials.

Still, much of the work to be done is on the demand side: families need to strengthen their financial position to better prepare for homeownership. This requires supporting families' efforts to increase their incomes, save for a downpayment, and maintain or repair credit scores, all of which can limit the risk of future loan defaults. Tightened lending standards, such as higher downpayments and stricter income verification, have made it more difficult for Millennials to qualify for a mortgage.[26] Unfortunately, the income of many Millennials is depressed because of a restrictive labor market that has hampered the generation's job prospects since the recession. Rates of un- and underemployment for young workers is always higher than for the general population, even in times of economic booms, but this already-heightened rate of unemployment for young workers has been magnified by the effects of the Great Recession.[27] In addition to having low and unstable income streams, Millennials have higher levels of debt, especially in the form of student loan debt, compared to previous generations of young people. In 2010, 41 percent of households under age 30 held student loan debt, compared to 30 percent in 2004, and the amount of debt has increased.[28]

At the same time as less money is being saved by Millennials, more money is being required by lenders for a downpayment. If the rising cohort of young adults cannot improve their balance sheets by increasing their savings and lowering their liabilities, they will be denied access to one of the most historically powerful asset-building tools—appropriate mortgage financing. Further policy solutions will be required to address the inequities in current policy, typified by the mortgage interest deduction, and to reexamine how access to housing finance can embrace the diversity of America. Responding to these challenges can play a constructive role in expanding the opportunity of ownership in America for the rising generation of Millennials.

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Endnotes

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[4] William R. Emmons and Bryan J. Noeth, "Housing Crash Continues to Overshadow Young Families' Balance Sheets," *In the Balance: Perspective on Household balance Sheets*, Issue 7, February 2014, Federal Reserve Bank of St. Louis, 2014, p. 2.

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