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Where have all the RENTERS gone?

BY JACK C. HARRIS

Demand for Texas housing is booming. Last year, 213,000 homes sold through the state's multiple listing services and 123,000 single-family building permits were issued — both figures higher than in any year on record. In the midst of all this activity, however, is a multifamily housing market that is far from flourishing.

Apartment markets have been sliding for the past several years. Multifamily construction in Texas peaked in 1998, and now runs about 70 percent of that level. According to data from the National Real Estate Index, rents are down to 1997 levels in major Texas cities. Almost all multifamily housing is rental housing, and the Census Bureau indicates that rental housing vacancy rates in Texas rose to 14.1 percent in 2003 from a low of 7.9 percent in 1994.

One reason for the diverging fortunes of owner and rental housing is mortgage market conditions, which in recent years have greatly favored buying a home over renting. Interest rates are low, and Fannie Mae and Freddie Mac, the two heavyweights of the secondary mortgage market (where most home mortgage loans end up) are mandated to promote homeownership. Specifically, they are required by federal law to purchase a percentage of home loans tailored for "underserved segments of the population." This mandate has allowed many lower-income Americans to become homeowners for the first time, thus cutting into rental housing's traditional tenant base.

Even without low interest rates and easy credit, rental housing probably would have lost tenants. One of the advantages rental housing offers is relative freedom to move when the need arises. But as people age, they put down roots and move less often, making homeownership more attractive.

Data from the American Housing Survey (AHS), the most comprehensive set of data on housing available, can be used to test hypotheses about what is happening to rental markets. The survey is published by the U.S. Census Bureau and the U.S. Department of Housing and Urban Development every odd-numbered year. It is a national survey with totals inferred from small but geographically extensive samples. Although the AHS is not specific to Texas and is not up to the minute (the most current data are for 2001), this data set provides insight into the market as a whole and leads to some surprising conclusions.

Hypothesis: Easy access to homeownership is attracting higher-income tenants away from rental housing. By lowering the threshold cost of becoming a homeowner, low interest rates have reduced the income level required to buy a home. This means many households whose income used to be too low can now afford to buy, taking them out of the rental market. Vacancies have risen and rental rates have been lowered to accommodate less affluent tenants, thus lowering rental income.

Trends documented by the AHS from 1991 through 2001 show that the opposite happened. During the period, the overall homeownership rate (percentage of households that own their homes) increased by 3.8 percentage points (from 64.2 to 68 percent). However, for households with incomes from $30,000 to 35,000 (the high end for renter households), the homeownership rate actually fell by 2 percentage points, while the rate for those with incomes of $10,000 to 20,000 rose slightly by 1.8 points from 1993 to 2001. The fastest-growing group among renters is households with incomes of $30,000 to 35,000.

Singles Defect to Homeownership When Values Rise

Period	Percentage Change During Period		
	Single Households	Single Renters	Home Market Value
1991–1993	2.7	0.4	4.4
1993–1995	4.7	4.8	2.8
1995–1997	5.0	0.6	7.1
1997–1999	6.5	3.9	9.6
1999–2001	4.6	0	12.9

Sources: U.S. Census Bureau and Office of Federal Housing Enterprise Oversight

So, easy mortgage credit apparently is allowing the *least* affluent tenants to buy homes.

Hypothesis: Married couples are able to buy homes at a younger age and, therefore, rely on rental housing to a lesser extent.

There is good evidence to support this claim. From 1991 to 2001, the rate of homeownership among married couples under the age of 25 rose by 11 percentage points (from 26.8 to 37.8 percent) while the overall homeownership rate went up a little less than 4 percentage points. The rate for married couples from 25 to 29 years old rose by more than 8 percentage points. As a consequence, the number of married renters went down by almost 12 percent at a time when the overall number of married couples was growing by 8 percent. The number of married renters between the ages of 25 and 29 shrunk by more than 31 percent.

Hypothesis: In recent years, singles have been buying homes, largely attracted by good investment returns.

The table contrasts the growth in single households overall and that of single renters from 1991 to 2001. Also shown are U.S. home appreciation rates as measured by the Office of Federal Housing Enterprise Oversight's House Price Index. In years when appreciation rates are high, few newly formed single households become renters.

Presumably singles are buying homes because of the attractive investment return. Singles make up almost 38 percent of the rental housing market, so if they turn to homeownership in large numbers, demand can be seriously hampered.

Hypothesis: More renters are choosing to rent single-family homes.

If single-family homes are defined as detached homes, this premise is totally false. From 1991 to 2001, the number of renters in single-family detached homes fell by 6.1 percent. Even harder hit were two-to-four unit buildings; the number of renters in these declined by almost 8 percent.

On the other hand, the number of rental townhomes increased by 31.7 percent, the largest growth rate for any type of structure. Once touted as affordable owner-occupied housing, single-family condos were being converted back to rental housing at a rapid pace. Apparently, those who desired a detached home were able to buy one.

Hypothesis: Fewer are renting because of reduced rates of mobility.

Mobility, the tendency to change residences frequently, is a major reason many people choose to rent rather than buy. If fewer households are moving, homeownership becomes more attractive. There is some support for this notion, as the percentage of households reporting a move during the previous year has declined somewhat in recent years.

The percentage remained steady from 1991 to 1997 at 17.6 percent. Since then, it has fallen to 16.1 percent. This is not a compelling trend, but may have contributed some to the rise in homeownership.

Hypothesis: Rising prosperity has brought homeownership within reach for more households.

As mentioned previously, it is not higher-income tenants who are leaving rental housing. Rather, it is those with lower incomes, and younger married couples. This shift is reflected in the growth rates of household income for homeowners and renters over the period.

Renter income grew by 2.8 percent from 1991 to 2001 while homeowners earned 1.9 percent more. From 1997 to 2001, when homeownership rates accelerated, the difference was even greater: 4.1 percent for renters and 2.5 percent for owners. Homeowners earn much more than renters, but the ratio of renter-to-owner income has remained around 53 percent since 1997.

It is no surprise that rental housing has lost some of its appeal in recent years. Low interest rates and liberal mortgage underwriting have opened the door to homeownership for a broader range of households, many who have traditionally relied on rental housing.

Impressive appreciation rates and enhanced tax benefits, such as the ability to avoid tax on resale profits, make homeownership smarter than ever. Consequently, rental housing has lost significant numbers of lower-income households, young married couples and singles.

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