

*California Real Estate Economics, 3<sup>rd</sup> Edition, Update*  
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**Chapter 16: Real Estate Trends in California**

- I. Affordable Housing in California
  - A. In the past 30 years, California's housing prices have out paced people's income.
    1. One in five households can afford a typical house in California.
    2. The high cost of housing has led to overcrowding.
    3. More than 3 million California households pay more than they can afford for their housing.
    4. Federal government has reduced the number of programs for affordable housing.
  - B. Affordable housing development
    1. Affordable housing is still funded by the Federal government, but now required greater private investment.
    2. Affordable housing also requires greater local government participation.
    3. Many communities no longer welcome population growth as they once did.
    4. Hostility feeds and strengthens certain myths and perceptions about affordable housing.
    5. Myths and perceptions maybe positive, but the negatives are usually highlighted to discourage growth. Such perceptions include:
      - a. Traffic will become unbearable.
      - b. Schools will become overcrowded.
      - c. Criminal element will be attracted.
      - d. New buildings will clash with existing buildings.
    6. Affordable housing makes economic sense:
      - a. More units per acre must lower the cost per unit.
      - b. Density bonuses are given to developers.
      - c. Smaller units cost less than larger ones.
      - d. People who live in affordable units own fewer automobiles and drive less.

7. In California, in the sixth largest metropolitan areas, 2/3 of renters and over ¾ of the households living below the poverty line own no vehicles or only one car.
  8. With lower car ownership rates come fewer trips and fewer single-occupant commuters.
- C. High density vs. economics
1. High density can encourage nearby retail development along with commercial development and ease of walking and transit use.
  2. Mixed housing with commercial development becomes more crucial with today's gasoline prices.
  3. ¾ of the vehicle trips in Southern California are non-work related.
  4. Stores serving neighborhood residents are likely to move into these high density neighborhoods.
  5. Transit connections become more common when neighborhood density increases.
- D. Case studies
1. San Diego (Little Italy)
  2. City of Los Angeles and moratorium on condominium conversions
  3. Between 2001 and 2003, the City of Los Angeles planning department had not received any applications for condominium conversions.
  4. In 2004, the City of Los Angeles approved 1,083 applications. Then dropped to 1,025 in 2005, and 899 in 2006.
- E. When one community does not concur with another.
1. City of Anaheim adopted an overlay zone that would allow the development of residential units in conjunction with hotels.
  2. In 2007, the Anaheim Planning Commission voted to deny a proposal on Katella Avenue for affordable housing.
  3. During the height of the condominium craze in So. California, the multifamily housing market in Orange County remained one of the strongest in the United States.
  4. New development in Orange County has primarily focused on Class A properties, which offer an array of amenities.
- F. What is the state doing about housing?
1. Senate Bill SB 1227 placing Proposition 46 on the November 5, 2002 ballot, approving \$2.1 billion in state general Obligation Bonds for housing.

2. The Department of Housing and Community Development (HCD) and the California Housing Finance Agency (CalHFA) are to utilize the \$2.1 billion to build and improve housing throughout California.
  3. Persons at risk are identified in the general plan's housing element.
- G. The housing element of the general plan
1. State law requires that every city and county must prepare and adopt a housing element and must include the following:
    - a. Identification and analysis of existing and projected housing needs.
    - b. An identification of resources and constraints to address these needs.
    - c. Goals, policies and scheduled programs for the maintenance, improvement, and development of housing for all economic segments of the community.
  2. California state law was amended pursuant to Government Code Section 65008, which requires the following in the preparation and the adoption of a housing element:
    - a. As part of a governmental constraints analysis, a housing element must analyze potential and actual constraints upon development, maintenance, and improvement of housing for persons with disabilities.
    - b. The housing element must include programs that remove constraints or provide reasonable accommodations for housing designed for persons with disabilities.
  3. According to HCD, the following questions should be asked when analyzing a housing element as it relates to removing constraints on development:
    - a. Does the city/county have any processes for individuals with disabilities to make requests for reasonable accommodations with respect to zoning, permit processing, or building laws?
    - b. Describe the process for requesting a reasonable accommodation.
    - c. Has the municipality made any efforts to remove constraints on housing for persons with disabilities?
    - d. Does the municipality make information available about requesting reasonable accommodations with respect to zoning, permit processing, or building laws?

- e. Has the city/county reviewed all of its zoning laws and policies for compliance with fair housing law?
  - f. Are residential parking standards for persons with disabilities different from other parking standards?
  - g. Does the municipality restrict the siting of group homes?
  - h. What zoning districts provide for group homes other than residential zones covered by state law, and are group homes over six people allowed?
  - i. Does the municipality have occupancy standards in the zoning code that apply specifically to unrelated adults and not to families?
  - j. Does the occupancy standard comply with fair housing laws?
  - k. Does the land use element of the general plan regulate the siting of special needs housing in relationship to one another, specifically is there a minimum distance between two or more special needs housing establishments?
  - l. How does the municipality process request to retrofit homes for accessibility?
  - m. Has the municipality adopted the Uniform Building Code?
  - n. Has the municipality adopted any universal design elements in the Building Code?
  - o. Does the municipality provide reasonable accommodations for persons with disabilities in the enforcement of building codes and the issuance of building permits?
4. The State of California reviews and assists local cities and counties in preparing goals and policies as well as programs for the implementation of housing element law.
- H. Other solutions to housing in California
- 1. Encouraging the development of second units/granny units
  - 2. Second Unit Law
  - 3. 1982 a milestone for second units in California
  - 4. No environmental review required for second units in California
  - 5. Implication of restrictions
    - a. 1984 decision of *Hubbart v. County of Fresno*
    - b. 2000 decision of *Coalition Advocacy Legal Housing Options v. City of Santa Monica*
  - 6. The economics of second units

- a. They provide affordable housing.
- b. They allow for potential supplemental income for homeowners.
- c. Manufactured homes can also serve as second units in rural areas, greatly reducing the cost of the units.

## II. Government Enters the Business of Real Estate Redevelopment

### A. Introduction to redevelopment

1. Redevelopment is the primary tool used by cities in California to revitalize deteriorating and blighted neighborhoods.
2. Redevelopment is used by over 1/3 of counties and 2/3 of cities in California.
3. Redevelopment law in California was adopted in 1945 as the Community Redevelopment Act.
4. In 1952, the voters approved tax increment financing
  - a. This tax increment financing weaned government away from loans and grants.
  - b. By 1965 only 46 redevelopment agencies existed
  - c. By 1975, 158 redevelopment agencies had been established.

### B. What is redevelopment?

1. Redevelopment is the process and program of activities undertaken by local governments to deal with the impact of blight and slum
2. Blight is a legal term that encompasses a list of conditions, and is a prerequisite for the adoption of a redevelopment agency.
3. Under Redevelopment Law, blight includes:
  - a. Buildings that are unsafe or unhealthy for occupancy
  - b. Factors that hinder or prevent economic viable use of buildings or lots caused by substandard design
  - c. Incompatible uses that prevent economic development
  - d. Subdivided lots or irregular form and shape or inadequate size for proper usefulness
  - e. Depreciated or stagnant property values or impaired investments, including properties that contain certain hazardous wastes
  - f. Abnormally high vacancies, abnormally low lease rates, abandoned buildings or excessive vacant lots

- g. Lack of necessary commercial facilities that are normally found in neighborhoods, including grocery stores, drug stores, and banks, and the like
  - h. Residential overcrowding or an excess of bars and liquor stores or other businesses catering to adults
  - i. High crime rates that constitutes a serious threat to public safety and welfare
  - j. Lack of adequate public infrastructure
- C. How is redevelopment implemented?
- 1. Only cities and counties have the authority to establish a redevelopment agency.
  - 2. Typically the City Council or Board of Supervisors act as the governing body of the redevelopment agency.
  - 3. The actual administration of the redevelopment agency is done by staff of the agency.
- D. What does redevelopment do?
- 1. Redevelopment agencies undertake a variety of projects and activities design to improve a project area and eliminate blight:
    - a. Downtown revitalization
    - b. Retail development
    - c. Industrial development
    - d. Residential development
    - e. Public facilities
- E. How is redevelopment achieved?
- 1. A redevelopment agency has a variety of powers granted to it under the state's constitution, which include:
    - a. Organize its affairs and staffing to carry out the redevelopment plan
    - b. Adopt a budget and system to pay and account for expenditures
    - c. Buy property
    - d. Sell property
    - e. Make loans or grants to carry out the redevelopment plan
    - f. Construct improvements on property
    - g. Construct infrastructure and other public improvements

- h. Assist development by property owners, developers or manufacturing companies to carry out the redevelopment of the area consistent with the redevelopment agency's adopted plan
      - i. Assist development or rehabilitation of housing for use by moderate to low income families.
    - 2. A redevelopment agency has the ability to buy private property for resale
    - 3. A redevelopment agency has the power of eminent domain
    - 4. A redevelopment agency has the power to collect property tax increment.
    - 5. The "no's" of redevelopment are:
      - a. No new taxes
      - b. No new assessments
      - c. No new fees
  - F. Examples of successful redevelopment
    - 1. The Downtown Plaza Mall in Sacramento, Ca
    - 2. Hollywood, Ca
  - G. Summary of redevelopment
    - 1. California's redevelopment agencies can transform local communities where decay, destruction and general sense of hopelessness reside.
    - 2. California Constitution provides redevelopment agencies the ability to collect tax increment
    - 3. Property tax increment is the primary source of revenue for redevelopment agencies.
    - 4. Redevelopment agencies use their authority to issue long-term bonds to finance projects
    - 5. In 2002, redevelopment agencies statewide collected \$2.5 billion in tax increment revenue.
    - 6. \$15 out of every \$100 of property tax revenue of the assessed value of all property in the state.
    - 7. California's 384 active redevelopment agencies have 764 project areas.

### III. Smart Growth

- A. Smart growth: the future of real estate development

1. One of the hottest trends in land use and real estate development, is the conservation of natural resources, which is referred to as smart growth
2. Example of resources include:
  - a. Natural lands
  - b. Critical environmental areas
  - c. Protection of water resources
  - d. Air quality
  - e. The reuse of already developed land
3. The attempt to conserve natural resources by reinvesting in existing infrastructure and reclaiming historic buildings
4. Smart growth is all about how we build our communities.
5. Smart growth principles include the following:
  - a. Mixed land uses
  - b. Take advantage of compact building design
  - c. Create a range of housing opportunities and choices
  - d. Create walkable neighborhoods
  - e. Foster distinctive, attractive communities with a strong sense of place
  - f. Preserve open space, farmland, natural beauty, and critical environmental areas
  - g. Strengthen and direct development toward existing communities
  - h. Provide a variety of transportation choices
  - i. Make development decisions predictable, fair, and cost effective
  - j. Encourage community and stakeholder collaboration in development decisions
6. Environmental benefits of smart growth
  - a. Minimize air and water pollution
  - b. Encourage brownfield cleanup
  - c. Preserve natural lands
  - d. Reduce greenhouse gases
  - e. Encourage compact development
  - f. Reduce impervious surfaces

- g. Improved water detention
  - h. Better transit accessibility
  - i. Better pedestrian and bicycle development.
- B. Examples of smart growth
- 1. Hismen Hin-Nu Terrace, Oakland, CA
  - 2. Downtown Brea, Brea, CA
  - 3. Uptown District, San Diego, CA
  - 4. The Crossings, Mountain View, CA
- C. Compact Development Endorsement Program, San Francisco Bay Area Communities
- 1. Green Belt Alliance
  - 2. Mixed use developments
  - 3. Affordable Housing Projects
  - 4. Endorsements from the Green Belt Alliance include projects in:
    - a. San Jose, Ca (Rylands Mews)
    - b. Emeryville, CA (Warehouse Lofts)
    - c. Barrio Logan, San Diego, CA (residential community)
    - d. Central District Specific Plan, City of Pasadena, CA
    - e. Accessory Unit Program, Santa Cruz, CA
- D. Smart growth trends and opportunities
- 1. Infill redevelopment is a high priority investment strategy for developers.
  - 2. Revitalization of Main Streets
  - 3. 37 out of the 40 metropolitan areas in the U.S. are constructing new rail lines.
  - 4. 71% of older households want to live within walking distance of transit.
  - 5. Bank of America has expanded its commitment to smart growth projects.
  - 6. 14 million new households will want to locate within ½ mile of transit facilities by 2050
- E. The present and the future
- 1. Future homebuyers are becoming environmentally conscious.
  - 2. Real estate agents should become familiar with smart growth principles.

3. Real estate agents should become familiar with green building programs such as the LEED program.
  4. Water and energy efficiency.
- F. What is green building?
1. Green building is defined as applied common sense.
  2. Three fundamental objectives of green building involve:
    - a. Conserving natural resources
    - b. Increasing energy efficiency
    - c. Improving indoor air quality
- G. Benefits of green building
1. The environment
  2. Building more efficiently, healthy building
  3. Creating environmentally friendly image for businesses
  4. The ability to market the services of a real estate professional
  5. Higher quality, environmentally sound products:
    - a. Recycled content decking
    - b. FSC-certified wood
    - c. Engineered lumber
    - d. Interior steel studs
    - e. Solvent-free adhesives
    - f. Natural linoleum flooring
    - g. Recycled content ceramic tile
    - h. Flyash in concrete
    - i. Bamboo flooring
  6. More durable/lower maintenance products
    - a. Fiber cement siding
    - b. Recycled content decking
    - c. Exposed concrete flooring
    - d. Natural linoleum flooring
    - e. Recycled content ceramic tile
    - f. Resource efficient landscape gardens
    - g. 40-year roofing

7. Products and practices that provide greater comfort and lower utility bills
  - a. Foundation/slab insulation
  - b. Increased wall and ceiling insulation
  - c. Spray cellulose insulation
  - d. Advanced infiltration reduction practices
  - e. Low E windows
  - f. Hydronic heating
  - g. All ducts located in conditional spaces
  - h. Ceiling fans
  - i. Whole house fans
  - j. Passive solar heating
  - k. Natural cooling
  - l. Energy star appliances
  - m. Attic ventilation systems
8. Healthier products and practices for families
  - a. Low/No VOC paints
  - b. Natural linoleum in place of vinyl flooring
  - c. Formaldehyde free medium density board (MDF)
  - d. Solvent free adhesives
  - e. Water-borne wood finishes
  - f. Clean ducts before occupancy
  - g. Exhaust fans in attached garages
  - h. Recycled content fiberglass insulation with no added formaldehyde
  - i. Seal all particle board
9. Who has green building programs/incentives?
  - a. City of Santa Barbara
  - b. County of Alameda
  - c. These programs provide assistance and guidance
  - d. Market appeal and support
10. Monetary incentives
  - a. Expedited permit processing

- b. Location-Efficient Mortgages (LEMs)
- 11. LEMs
  - a. Increase borrowing capacity
  - b. Recognize transportation savings
  - c. Encourage borrowers to look at transit oriented developments
- 12. Where are LEMs currently offered?
  - a. San Francisco Bay Area
  - b. Los Angeles
  - c. Orange County
  - d. Seattle
  - e. Chicago

IV. The State of the Real Estate Market

- A. Subprime loans
  - 1. Qualified borrowers with credit scores below 620
  - 2. Borrowers will face foreclosures
  - 3. Adjustable rate mortgages (sub prime)
  - 4. Delinquency rate provides measure of potential down side
    - a. Delinquency rates provide measure of downside of market
    - b. Loans posing greatest risk are those originated in 2005 / 2006
    - c. Payment resets are potentially sending borrowers into foreclosure
    - d. Foreclosure rates in 2006 ranged from 7.3% in Barnstable-Yarmouth, Mass. to 21.6% in Merced, CA of all mortgages.
  - 5. What are the implications of the subprime market to the economy
    - a. Subprime borrowers with poor or questionable credit histories were able to use a combination of rising home prices and easy credit to live beyond their means.
    - b. Low interest rates led to fueling the economy.
    - c. Default of subprime mortgages have resulted to tightened credit standards.
    - d. Low interest rates led to boom in home equity loans and so-called cash-out mortgage refinancing replacing old loans

with new loans and taking out some of the homeowner's equity.

- e. Home equity cash-outs resulted in approximately 48% of the money spent on investments, including home renovations and education; 44% on gifts and living expenses and travel.
  - f. As a result of reduced access to credit, economists are forecasting tough times for retailers.
  - g. Slower home appreciation
  - h. Tighter lending standards
  - i. The national foreclosure rate in April 2007 was one new filing for every 783 households.
  - j. Freddie Mac to buy over several years \$20 billion of subprime loans to be held in its portfolio.
6. Who leads in subprime lending?
- a. Washington Mutual
  - b. Citigroup, Inc.
  - c. Countrywide
  - d. Wells Fargo
  - e. J.P. Morgan Chase & Company
7. Risks
- a. Loans for investment properties carry more risk due to potential for abandonment.
  - b. Many of the loans made were adjustable rate mortgages.
  - c. Many of the loans were optional adjustable rate mortgages, giving borrowers the choice of payments/schedules.
  - d. Many loans only covered part of the interest and no principal.
  - e. Speculators did not foresee the slow down in the housing market.

V. Summary

- A. California became ground zero for developers to accommodate a changing market.
- B. The high cost of housing and traffic has led to the desire to becoming more environmentally conscious.

- C. Within 5 to 10 years, urban cores will see greater housing densities and more affordable housing units.
- D. Limited supply of land and stringent entitlement requirements in California will continue to push the cost of housing upward.
- E. Developers are likely to shift toward high-density projects
- F. Young people in their 20s and 30s will chose more affordable urban core developments that are close to their employments.
- G. As the single-family housing market cools in California, the next investment is likely to be apartments.
- H. The National Association of Home Builders Housing Market Index (HMI) gauges builder's perception of future home sales.