Solving the Home Affordability Crisis

A GUIDE FOR POLICYMAKERS & LOCAL GOVERNMENT LEADERS
In Seattle, the median home price is $830,000—a 14 percent increase compared to 2017. In Oakland, it’s about $757,700, a 12.2 percent year-over-year increase. In Austin and Raleigh, current median home prices are approximately seven to eight percent higher than in 2017.

As a result, a growing number of middle-income earners—or a family of three earning between $42,000 and $125,000 per year, according to Pew Research—struggle to purchase homes. Recent research indicates one-third of Americans spend more than 30 percent of their income on housing. In some metro areas, between 33 percent to 50 percent of all households can’t afford payments on a median-priced single-family home.

Federal, state and local housing programs typically focus on low-income populations—and rightfully so. But the fact that many middle-class Americans can no longer afford to buy a home has serious implications for both citizens and communities. Homeownership historically is an important method...
to build wealth. It’s also a source of stability and kinship for communities that helps unite diverse populations toward common goals.

The importance of homeownership is reflected in the results of a national research survey conducted by the Governing Institute to support this guide. More than 40 percent of government officials surveyed said the nation faces a housing crisis, and another 33 percent called affordability a serious challenge. Citizens responding to the survey had a similar — if somewhat less dire — view of the issue. About 50 percent of citizen respondents called housing affordability either a crisis or a serious challenge.²

It’s surprising this number is not higher. April 2018 marked the 74th consecutive month the median home price in the U.S. increased, while inventory of existing homes declined for 35 straight months. Experts expect the problem to get worse, forecasting U.S. home prices to rise 4.5 percent in 2019 and another 3.6 percent in 2020.³

Making homeownership affordable for more Americans is a complex issue and addressing it will demand a multi-faceted approach involving legislation; housing innovation; public-private partnerships; and targeted efforts at the federal, state and local government level.

In Seattle, the median home price is $830,000.
Homeownership is far and away the most prominent driver of wealth in the U.S. economy,” notes Ben Hecht, author of “Reclaiming the American Dream: Proven Solutions for Creating Economic Opportunity for All.”

Appreciation in value, the ability to leverage and a forced-savings mechanism by way of equity all combine to make homeownership one of the most reliable long-term investments an individual can make in his or her lifetime. According to the Federal Reserve Bank, the 2016 median net worth of a homeowner was more than 44 times greater than that of a renter.\(^4\)

The inability to purchase a home is debilitating not just to current prospective buyers, but to future generations — a fact evidenced by the severe racial wealth disparities that exist in the U.S. today. As Hecht notes, decades of public and private financing policies and practices that denied or severely restricted homeownership along racial lines are still impacting people of color. Homeownership rates among white families stands at 71 percent as of 2016, while the same is true for just 47 percent of Hispanics and 41 percent of blacks. According to a 2015 study, if blacks and Latinos were as likely as white households to own their own homes, the wealth of black households would grow by more than $30,000 and the wealth gap between these two races would shrink 31 percent.

Notes Hecht: “If low-income people and people of color continue to face systemic challenges to this critical wealth-building opportunity, there is no reason to expect that monstrous wealth gaps will not continue to widen.”\(^5\)

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*Ben Hecht, Author, “Reclaiming the American Dream: Proven Solutions to Creating Economic Opportunity for All”*
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WHY IT’S SO DIFFICULT TO PURCHASE A HOME

“...The cost to buy a home is about 70 percent more than the typical household can afford.”

Darin Ranelletti, Policy Director for Housing Security, City of Oakland

EXPLODING POPULATION GROWTH INCREASES HOUSING DEMAND.

In many parts of the country, it’s an issue of supply and demand. Seattle, for instance, doesn’t have enough houses.

“We’re dealing with a period of unprecedented growth, both in the city of Seattle and in our metropolitan region,” says Steve Walker, director of the Seattle Office of Housing. “Fifty-seven people move here every day. We began with a deficit of affordable homes, as we emerged from the Great Recession. We’re dealing with demand that’s overwhelming supply and fueling displacement of low-income residents and communities of color.”
Rapid job growth in Oakland is causing the same problem in the San Francisco Bay Area.

“Since 1990, the Bay Area has added close to a million jobs and about half as many housing units,” says Darin Ranelletti, Oakland’s policy director for housing security. “The cost to rent an apartment is about 40 percent more than the average Oakland household can afford, while the cost to buy a home is about 70 percent more than the typical household can afford.”

Larger demographic trends also play a role. While homeownership rates among millennials — the largest generation in history — are beginning to rebound since the recession, baby boomers are living longer, aging in place and hanging onto their homes.

In addition, the gap between wages and housing costs is increasing. The housing shortage is pushing up the cost of homes, while wages are stagnant. Since the early 1970s, the hourly inflation-adjusted wages received by the typical worker have barely risen, growing only 0.2 percent per year.\(^7\) Meanwhile, the median home price increased 41 percent faster than inflation over the past three decades, according to the Joint Center for Housing Studies at Harvard University.

For example, in 1980, the median household income was close to $18,000, which was roughly 38 percent of the cost of the average home at $47,000. In 2018, the median household income is less than $50,000, which is only 22 percent of the cost of the average home at $220,000.\(^8\)

The housing market hasn’t fully recovered from the Great Recession.

The economic downturn and foreclosure crisis plays a significant role in today’s housing challenges.

According to the Federal Reserve Bank of Kansas City, home construction per household a decade after the bust remains near the lowest level in 60 years of record-keeping. The National Association of Home Builders estimates builders will start fewer than 900,000
new homes in 2019, less than the 1.3 million homes needed to keep up with population growth.9 “From 2007 to 2009, the market had collapsed; real estate values collapsed; builders stopped building. Housing starts fell dramatically and haven’t really recovered,” says Brad Blackwell, executive vice president of housing policy and homeownership growth strategies at Wells Fargo. “We’ve seen improvement in new construction, but we haven’t seen nearly enough.”

The foreclosure crisis also led to a tightening of the credit market, largely due to new federal regulations that create stricter underwriting standards for home loans. The goal of these regulations is to make homeownership more sustainable by ensuring people don’t buy a home they can’t afford, but a byproduct is that it also may limit access to credit for some first-time buyers and previously foreclosed homeowners who want to reenter the ownership market.

REGULATORY, LAND AND ECONOMIC ISSUES SUPPRESS HOUSING INVENTORY.
According to a National Association of Home Builders survey, 82 percent of construction professionals say availability of labor and materials costs are two of their biggest challenges.10 On average, the cost of materials rose 4.2 percent nationally in the first quarter of 2018.11 But regulatory and land issues also prevent state and local governments from increasing housing inventory. Land is scarce in major metro areas, which increases the need for diverse types of housing. However, zoning regulations can make developing inclusionary and diverse housing more cumbersome.
And current residents may oppose these efforts because they worry about increasing housing density. For example, 41 percent of citizen respondents to the Governing Institute survey said they would actively work against rezoning in their neighborhoods.

“We need to work on educating some of our residents that there are options that allow for a little bit of intensification, but not so much that it is now a four- or five story-apartment,” says Alan Stephenson, planning and development director for the city of Phoenix. “Unfortunately, we really haven’t had the political ability to tackle those types of housing projects.”

**Federal Housing Policy Typically Focuses on Low-Income Housing.**

Federal policy hasn’t focused directly on making homeownership affordable. Instead, these efforts have concentrated on the availability of low-income housing and tailoring federal regulations to create a more favorable credit and tax environment. But federal help may be crucial because state and local governments face growing budget constraints, and many will struggle to fund homeownership programs on their own.

Unfortunately, recent federal tax law changes — primarily the Tax Cuts and Jobs Act — may impact future homeownership rates. The law reduces the mortgage interest deduction and puts a cap on the amount taxpayers can deduct in state and local taxes — including property taxes — that could affect home affordability, particularly in states with a high cost of living.

All these factors combine to create a housing market that suffers from low supply and high costs — locking many Americans out of the housing market. Sixty-five percent of public officials responding to the Governing Institute survey said available properties in their communities are too expensive for first-time buyers and the same percentage said increasing housing inventory in their communities is a high to very high priority.

“There are a lot of families and individuals who are renting now, who in a more fully functioning or healthier housing market, would be homeowners,” says Stockton Williams, executive director of the National Council of State Housing Agencies (NCSHA). “This would allow them to begin to build wealth, because for better or worse, owning a home is still the primary means by which most people do that in this country. In a lot of ways, solving the housing affordability crisis in America begins with creating more affordable first-time homeownership opportunities.”
SOLUTIONS TO INCREASE HOMEOWNERSHIP

Housing is a regionalized and localized issue, so this challenge differs across the country. But most government officials (60%) surveyed by the Governing Institute said their jurisdictions have ongoing initiatives to alter or modify policies and practices to make homeownership more affordable. And a whopping 82 percent of citizens surveyed said government should be involved in affordability efforts.

City officials say they are trying a range of solutions to improve housing affordability.

Overall, municipalities are finding ways to incentivize builders, address land scarcity, overcome restrictive zoning regulations, build a funding pipeline and more.

INCENTIVIZING BUILDERS

There’s plenty of construction happening in San Jose — just not the kind that produces affordable homes. Instead, a booming commercial real estate market is jacking up land prices and creating a shortage of construction labor. Mayor Sam Liccardo says the city changed its fee structure to help developers who are interested in constructing lower-cost homes.

“More than 20 million square feet of office and R&D (research and development) space has been under construction for the last couple of years in this metro area,” Liccardo says. “As long as construction labor and resources are sucked into building large corporate campuses, it makes it all the more expensive for any housing developer to get bids to build anything. We’re trying to do what we can to work within the market, and that means enabling affordability by design.”

Liccardo says city leaders are encouraging what he calls a “smaller and taller approach,” where developers increase the density and reduce the square-footage of housing units.
60% OF CITIZEN RESPONDENTS TO THE GOVERNING INSTITUTE SURVEY SAID THEY WOULD SUPPORT SMALLER HOUSE CONSTRUCTION IN THEIR OWN NEIGHBORHOODS.
“Obviously, it requires incentivizing developers,” he adds. “For example, if fees are calculated on a per unit basis, there is very little incentive for developers to densify and build smaller units, so we’ve adjusted our fees to a square-footage basis. That encourages builders that are building more to that market.”

In Minneapolis, the mayor’s office is exploring ways to more broadly distribute lower-cost housing in the city. Currently there is a $25,000 per-unit cap on subsidies for developers within the affordable housing trust fund — an amount too low for them to buy land and build in Minneapolis’ more affluent areas. Peter Ebnet, senior strategic policy advisor to Minneapolis Mayor Jacob Frey, says the city is considering removing the cap, which would better enable developers who want to build in higher-cost areas to do so.

Nearly 44 percent of government respondents to the Governing Institute survey said they preferred incentivizing developers to make housing more affordable, compared to other options like requiring builders to allocate more low-income housing in their construction or rezoning.

### ADDRESSING LAND SCARCITY

Many cities are looking to community land trusts to unlock local land supply. Community land trusts are nonprofit, community-based organizations that purchase land to preserve local affordable housing. About 225 community land trusts are active in the U.S., which represent about 15,000 affordable homeownership units. These organizations have developed largely in response to gentrification and represent efforts to preserve cities’ cultural and socioeconomic diversity.

In addition, cities like Phoenix are working with developers to build affordable homes on city-owned lots. Phoenix’s housing department accumulated nearly 700 residential lots during the recession. Now the city is awarding some of these lots to homebuilders with the caveat that they sell to first-time buyers who are at or below 80 percent of the area’s median income, says Cindy Stotler, director of the department. The city also awarded 30 city-owned residential lots to Habitat for Humanity to rehab and sell to first-time and low-income buyers.

“We’re trying to get rid of any land we own because we know that either giving away or heavily discounting land is a way to incentivize affordable housing,” Stotler says.

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**POLICY PREFERENCES**

As a government official, which of these options would you prefer to see implemented to make housing more affordable?

- **Incentivize Developers**: 44%
- **Require Builders to Allocate Low-Income Housing**: 43%
- **Rezone Properties**: 37%
- **Improve Public Transit**: 36%
- **Allow for Smaller House Construction**: 36%
- **Reduce or Remove Development Regulations**: 23%
Issues with housing supply and demand aren't just unique to the homeownership market. High housing costs and high rent structures in many communities have created a growing need for affordable rental housing as well.

In addition to efforts to address land scarcity, restrictive zoning regulations and high construction costs, helping developers, nonprofits and other organizations access capital to build affordable housing is one approach that has increased housing options in areas where costs are skyrocketing.

Wells Fargo, the top investor in affordable, multifamily housing in the country and an active lender for affordable housing projects, works with these groups to fund affordable housing projects with both debt and equity, primarily through its Community Lending and Investment group. Wells Fargo has lent more than $13 billion to finance the construction or rehabilitation of affordable housing properties since 2014. The primary mechanism by which Wells Fargo provides equity for affordable housing projects is through federal Low Income Housing Tax Credits (LIHTC), and since 2012, Wells Fargo has invested nearly $11 billion in LIHTC equity. Wells Fargo provides equity support by purchasing low-income housing tax credits awarded to developers for qualified housing projects. This gives the bank an equity stake in the project and allows developers to access much-needed capital. With this approach, developers don’t have to take on as much debt to construct new housing, allowing them to charge below market-rate rents and create more affordable units.

“The housing brings lower rents to serve low- and moderate-income people in our communities,” says John Epstein, executive vice president for community lending and investment debt at Wells Fargo. “This housing sometimes has a specific focus. It may focus on providing housing for veterans, families recently coming out of homelessness, people who are working at moderate or lower-income jobs or seniors. It’s a platform that promotes and brings financing alternatives to the local communities where we are involved.”

One recent success is the Essex Crossing project in Manhattan. Wells Fargo has provided more than $400 million in financing for the $1.5 billion project, which will include mixed-income housing, health care facilities, cultural and entertainment attractions, office space, parks and retail on two million square feet of land that has been vacant for 50 years on the Lower East Side.

Wells Fargo worked with the project’s developers, Delancey Street Associates, and invested in the development by purchasing low-income housing tax credits and new markets tax credits, another federal tax credit incentive program that creates additional capital for commercial real estate projects. The financing has helped the developers take land that was empty for decades and convert it into mixed-use development and mixed-income housing. Six of the nine buildings on the site are currently under construction or complete, including a 14-story, 100-unit apartment building for affordable senior housing. Out of the 1,000 housing units that are part of the build, 500 units will be affordable housing.

This effort illustrates how creative partnerships can increase the supply of affordable housing. By working with developers and housing authorities, Wells Fargo has financed the creation of more than 200,000 units of affordable housing in the last six years. Partnerships like this are critical because the country faces an affordable housing shortfall of eight million units — for every 100 extremely low-income households, there are only 35 affordable rental units available.

Epstein says Wells Fargo has a team of more than 200 team members focused on community lending and investment and one of the largest affordable housing geographic footprints in the U.S.

“We have a huge commitment to this space — we’ve made a financial commitment, a team member commitment and a geographic commitment,” Epstein says. “We’re really trying to give back to communities and create more affordable housing.”
Another Phoenix project involves converting public housing into affordable homeownership opportunities. With the help of the U.S. Department of Housing and Urban Development (HUD) Section 32 public housing homeownership program, Stotler says her department is rehabbing 400 single-family public housing units and selling them at 20 percent of the appraised value to low-income buyers — some of whom may already live in them.

**OVERCOMING RESTRICTIVE ZONING REGULATIONS**

Inclusionary zoning policies — which require new residential developments to make a certain percentage of housing units affordable to low- or moderate-income residents — also will be key to increasing housing supply.

Montgomery County, Md., which passed one of the country’s first inclusionary zoning laws in the 1970s, has strengthened its policies over the last 40 years to create a more favorable environment for building affordable homes. Every residential development over 20 units — whether it’s rental housing or homeownership projects — must provide 12.5 percent moderately priced dwelling units, which are aimed at people who make around 65 percent of the area’s median income of $100,000.

Gwen Wright, the county’s planning director, says it’s important for municipalities to use zoning policies to promote more diverse housing types, or what’s known nationally as “Missing Middle Housing.”

“Generally, we’ve fallen into the system of only building single-family homes, townhouses or large multi-family dwellings,” Wright says. “This means there aren’t a lot of starter homes or condos for people to get their foot in the door in the real estate market and to build equity.”

The county recently completed a rewrite of its 40-year-old zoning code. Wright says leaders there are looking to build smaller apartments, condos, and side-by-side or two-over-two duplexes. This strategy could increase housing supply in high-density areas near transit. The county’s rewritten zoning code provides incentives for developers who include a mix of residential unit types and moderately priced dwelling units in their buildings.

The city of Minneapolis is considering a similar strategy. Ebnet says one proposal involves opening development on any single-family zoned lots to allow for greater housing options and flexibility of use. The city also passed ordinances to allow homeowners to build accessory dwelling units (ADUs) on their properties to house more people or to supplement their mortgage costs through rental income. In addition, the city promotes modular home construction to reduce construction costs and improve long-term affordability.

Seventy percent of government respondents to the Governing Institute survey said introducing new types of housing is necessary to address issues with housing inventory. Sixty-five percent of citizen respondents agreed, saying they would support neighborhood revitalization and housing investment in their neighborhoods. Sixty percent said they would support smaller house construction. All these strategies show movement in that direction and illustrate that tackling this part of the housing affordability challenge will require diverse solutions.

Despite this, many citizen survey respondents said they would actively oppose rezoning. It is important for government leaders to communicate with citizens about what will
and will not work for their neighborhoods, and how best to increase density without decreasing quality of life for current and future residents.

BUILDING A FUNDING PIPELINE

Some communities — including Philadelphia, San Jose, Oakland and Los Angeles — have established impact fees to fund affordable housing.

The fees are charged on market-rate development and go into an affordable housing trust. In San Jose, the fee is about $18 per square foot on new development, while Los Angeles recently approved a measure where developers will pay between $1 to $15 per square foot. City officials estimate the fee could raise $100 million per year for affordable housing in Los Angeles, where the median home value currently nears $675,000.

In 2016, the city of Denver passed an ordinance that established two funding sources to establish its affordable housing trust fund. Impact fees on new development projects and existing property tax are slated to dedicate $150 million over a decade to create or preserve at least 6,000 homes for low- and moderate-income families. In July 2018, Mayor Michael Hancock went further, saying he planned to ask the City Council to use marijuana taxes to double the affordable housing fund to $300 million.

“Within a year from now, we should be out buying more land, so that we can begin to work with some of our developers and community-based organizations that are building affordable housing.”

While many cities have housing trust funds, they can struggle to keep the coffers full — or ensure the money is not diverted to other interests. For example, for years the city of New Orleans used money from its Neighborhood Housing Improvement Fund on services like code enforcement instead of helping low-income families with housing costs. In St. Louis, voters approved a $5 million minimum annual allocation to the city’s affordable housing trust fund in 2002, but the city did not actually hit that number for six years in a row. And in Baltimore, 83 percent of residents voted in 2016 to approve a $3 million bond measure to establish the city’s affordable housing trust fund. However, it wasn’t until nearly two years later when city officials committed the first $2 million.

Baltimore housing advocates say much more is needed. One group is calling for the city to allocate $40 million from its general fund for community land trusts and to employ Baltimore residents to rehab vacant homes for resale. Though the city has approved another $10 million in bonds to support future affordable housing projects, the question is where Baltimore will get the money to sustainably fund its affordable housing trust fund long term. Current proposals call for increasing taxes on property sales to raise $20 million for affordable housing, but the taxes would only apply to sales of rental properties — a major sticking point that opponents say isn’t business-friendly.

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Gwen Wright, Planning Director, Montgomery County, Md.
Ultimately, long-term funding for affordable housing requires political leadership, community support and sustainable revenue sources. Impact fees can be a solution, but cities may need to balance these fees with other incentives for developers. Seattle gives developers the option of paying the fee or including affordable units within their developments. Montgomery County lets developers avoid paying some impact fees if they make 20 to 25 percent of the units in market-rate developments affordable. While these municipalities won’t generate the same amount of revenue to reinvest in affordable housing, the incentives help increase the number of housing units available to low- and moderate-income buyers.

**REINVESTING IN FIRST-TIME HOMEBUYER PROGRAMS**

Research shows that first-time homebuyer programs, especially those that include pre-purchase counseling, can improve mortgage literacy and empower buyers to take steps like correcting credit report errors that improve their chances of qualifying for a mortgage. 

With rising real estate prices, some cities have had to get creative with their first-time homebuyer programs. Oakland has raised the home purchase price limit for its program from $475,000 to $650,000, which gives more people the opportunity to participate if they meet the three-percent down payment requirement.

Milwaukee County, Wisc., recently launched a program called Opportunity Knocks. Through an ordinance, the county claims possession of foreclosed homes. It allows non-violent drug offenders to rehab the homes — providing job training in the process — and then sells them to first-time buyers through the county’s Section 8 Homeownership Program. The buyers receive down payment assistance to help with their purchase.

“It gives individuals an opportunity for housing mobility and social mobility to move to higher-opportunity neighborhoods. They’re finally affordable because we own the homes,” says James Mathy, the county’s housing administrator.

Partnering with mortgage lenders on these programs will also help municipalities increase home affordability to a wider pool of qualified buyers. One example is Wells Fargo’s NeighborhoodLIFT® program, where potential buyers can apply for down payment assistance from local nonprofits. Wells Fargo also offers the yourFirst Mortgage Program, where buyers can obtain a conventional fixed-rate mortgage with a three-percent down payment, which can come from a down payment assistance program. 

**COLLABORATING ACROSS FEDERAL, STATE AND LOCAL GOVERNMENTS**

Addressing housing affordability will require a collaborative response at the federal, state and local government levels.

At the federal level, this may mean even more of an investment than the government already has made — in 2015 alone, the federal government spent $190 billion to help renters and homeowners. According to the Center for Budget and Policy Priorities, this investment mainly occurred through tax subsidies like the home mortgage interest deduction. However, these benefits are no longer the same because of new limits implemented by the 2018 tax law.

As state and local governments face increasing budget constraints, federal funding could help ease some of the financial burden. Ebnet says Minneapolis is
advocating for more state funding and more federal funding from HUD.

“We’re hearing a lot from advocacy partners and developers that the city needs to put in more funding in general (into affordable housing),” he says. “The reality is that when the city puts in funding, most of our general fund comes from property taxes, so there’s always the concern that this could potentially drive up property taxes. Additional funding is critical.”

One possibility for additional federal funding could come from Opportunity Zones, which were added to the tax code as part of the new tax law. Opportunity Zones allow investors and developers to get preferential tax treatment for investing in economically distressed areas, which includes areas ranging from those with high poverty rates to communities with higher-than-average home price appreciation. The nature of these investments could be either commercial or residential development. It’s still too early to tell what impact Opportunity Zones will have in making communities more affordable, but if investments are made in residential housing, it could help ease some of the supply-and-demand issues that are driving up housing costs.

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Municipalities are trying a variety of approaches to make homeownership more affordable. As these cities demonstrate, there’s not one single, silver bullet solution for this challenge. Housing affordability is a local challenge that will require innovative solutions to make the American Dream of homeownership more accessible for future generations.

CONCLUSION

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Municipalities are trying a variety of approaches to make homeownership more affordable. As these cities demonstrate, there’s not one single, silver bullet solution for this challenge. Housing affordability is a local challenge that will require innovative solutions to make the American Dream of homeownership more accessible for future generations.

“Cities have traditionally been laboratories and incubators for new ideas. We have an extraordinary opportunity now to tackle what is a generational challenge,” says San Jose Mayor Liccardo. “We need to have the ambition to build a city for everyone in an era of rapid gentrification and a growing divide — that is the most important task of our age.”

SAM LICCARDO, MAYOR, CITY OF SAN JOSE

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