Housing for Middle-Income Wage Earners

Prepared by The Middlemarch Fund

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What is the Missing Middle?

The phrase missing middle housing (MMH) generally refers to middle class families. In terms of income levels, we often think of the missing middle as incomes that range between 80-120% of the area median income. While the income range varies depending on the number of people in a household, as an example, here in San Diego County in 2023, a family of two in the missing middle would earn $88,200 - $112,100, while a family of four would earn between $110,250 - $140,150.

This income range tends to include new college graduates, single persons, downsizing baby boomers, and millennials. These are people who work as teachers, government employees, police officers, middle management, customer service, and other such roles.

The word middle also refers to density, as these properties tend to have a lower perceived density, for example by making use of smaller units inside a building that from the outside matches the appearance of the neighborhood.

What Makes it Missing?

This type of housing is often labeled "missing" because most developers focus on building high-end housing where profits are easier to come by simply by charging higher rates to those who can afford them and in most cases to cover the rising costs of construction. Other developers focus on lower-income housing where profits can be protected through government subsidies. But without subsidies or the inability to pay whatever a developer needs to charge to make a profit, middle-income households simply do not get built.

Many more people would have their own home if not for the inability to afford one. Just prior to the COVID-19 lockdown, 32% of the adult population or approximately 79 million people were co-residing with someone unrelated to them. While some of those represent cohabitating romantic partners, it also includes approximately 24 million young adults who live with their parents and 34.6 million older adults living with an adult child. These are people who because they have a place to live are generally not considered when we think of those in need of housing... thus they too are “missing.”

Making it Affordably

High and/or medium density housing is less expensive because the infrastructure (water lines, waste lines, electricity, sidewalks, off-ramps, and other such features) are either already accounted for or can be spread out amongst more families.

Benefits

When it comes to specific neighborhoods, more desirable communities with greater resources benefit from the influx of tax dollars contributed by wealthier residents, while communities with fewer resources decline further. Without MMH, middle-income families are often forced to live in a resource poor but financially affordable community, or an amenity rich community that they can't afford. If they're able to manage to get into these higher quality neighborhoods, they quickly gain access to a myriad of benefits.

ESG Benefits

Missing middle housing incorporates social concepts (the S in ESG) by not only addressing the financial needs of tenants, but also building a stronger sense of community. When tenants find a place that they can afford and feel that their landlord respects them, it's only natural that they would stay longer and take better care of the property. This longevity and sense of personal responsibility leads to people feeling a part of the community.

Furthermore, turnover costs and vacancies are among the largest and most common operating expenses, and by significantly reducing theses expenses, investor returns are improved. One study found that in such situations, there was an 88% retention rate five years later.

> *"Equivalent to saving 183,280 barrels of oil or taking 14,536 cars off the road each year"*

Looking then at the environmental component (the E in ESG), missing middle and affordable housing which offer options that allow people to live closer to work and take advantage of public transit, are currently providing an annual reduction of 79,000 metric tons of carbon across San Diego County. This would be approximately equivalent to saving 183,280 barrels of oil or taking 14,536 cars off the road each year.

Health & Family Benefits

Studies have shown that resident health quickly improves upon moving into a more affordable property. In one report, residents began to use primary care 20% more often, ER visits dropped 18%, and total Medicaid expenditures were down 12% after just the first year. Another study found that over time, residents spent 23% fewer days in the hospital, had 33% fewer ER visits, spent 42% fewer days in assisted living facilities, and saved on average $6,000 per person per year.

On the other end of the economic spectrum, low-income neighborhoods are less safe and more stressful, have limited access to quality healthcare and healthier food choices, and are often closer to environmentally toxic sites such as industrial plants. Research confirms the health benefits of affordable housing. Missing middle and affordable housing programs in San Diego County annually save $36 million in pediatric care and $9 million in overall costs associated with obesity and diabetes.

Quality, affordable housing also helps to foster better parenting because adults are not forced to work multiple jobs to support their families. Conversely, living in unaffordable housing is associated with more absent parents, insufficient heating and cooling that distracts children from studying, and unsafe living conditions such as overcrowding or unclean premises that affect the physical and mental health of children and parents alike. Additionally, stressful living situations are associated with increases in child abuse and neglect. Studies have shown that incidents of abuse and neglect dropped by over two-thirds in families after moving into more supportive housing.

Additional Benefits

- Shorter commutes
- More family-time
- Children do better in school
- Less stress and anxiety
- Fewer physical health problems
- Frees up government-subsidized housing to address homelessness
- More diverse neighborhoods
- Stronger and more engaged communities
- Greater social equality
- More stable households
- More disposable income to save for homeownership or higher education
- Retention of skilled workers

Financial Benefits

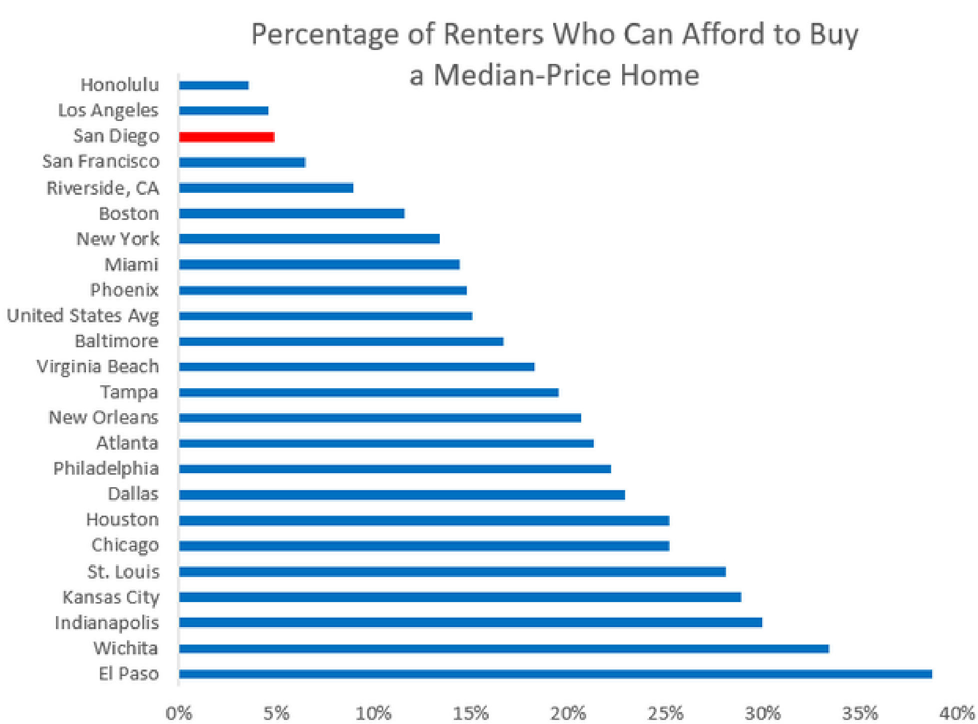
Given health and social benefits such as having a better learning environment and schools, along with a cleaner, safer home environment, children in San Diego County who grow up in affordable missing middle housing earn an average of $47,000 more in their lifetime. At the same time parents save money and live less stress filled lives. In fact, the median savings in rent per household in the county is $710/month.

San Diego County also benefits by having more people work here, which translates into over 24,000 jobs annually and an increase in state and local taxes of $257 million per year.

Missing Middle Housing also leads to more job opportunities, increased consumer spending, and economic growth in the region.

Buying vs Renting

When comparing household income to housing prices, San Diego has the worst “unaffordability score” in the nation. The total monthly payment necessary to purchase a median priced home in the San Diego region is $6,413, which requires an annual income of $248,247. This likely explains why only 4.9% of renters can afford to buy a median-priced home in San Diego.

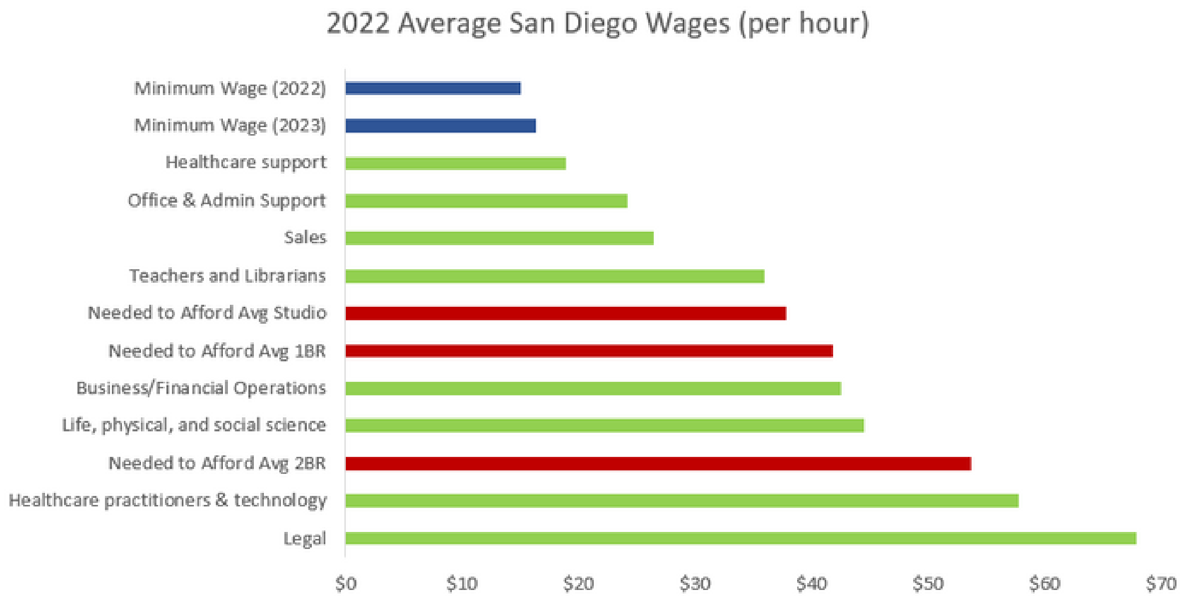


The inability of San Diegans to buy a home means that there will be more and more people opting to rent, and when the demand for rental properties increases so too will prices.

Monthly rents in San Diego shot up in the middle of 2021, with the annual increase peaking around 20%. Although the rate of increase began to drop in 2022, rent levels themselves remain at all-time highs. As a result, 57% of San Diego renters are now cost burdened, spending more than 50% of their income on housing costs. This combination of high for-sale and for rent prices explains why our region is in such dire need for more housing for our middle-income earners.

San Diego Employment

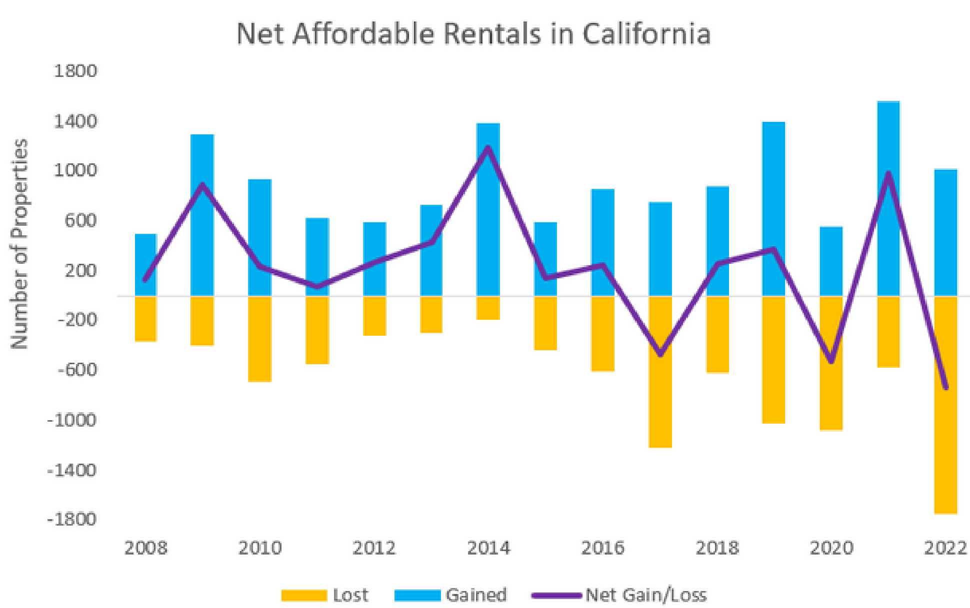
As mentioned above, San Diego salaries are lower than they are in other large cities in California, causing numerous San Diegans to either pack up and leave entirely or at least commute from outside the county, from places such as Tijuana and Riverside County. Compared to elsewhere in the state, wages for professional and office workers are 26% less, for firefighters they're 14% less, while attorneys are paid 32% less in San Diego.



Losing Affordable Housing

While new missing middle homes are built every year, others are lost. Keeping up with those losses is a constant battle. As we'll see shortly, even though in most years there is a net gain, those numbers fall well short of the need, making every loss that much more impactful.

Currently, 31,309 homes are at risk of being converted into market rate units between 2023 and 2033, with 70% of those anticipated losses expected in the next five years.

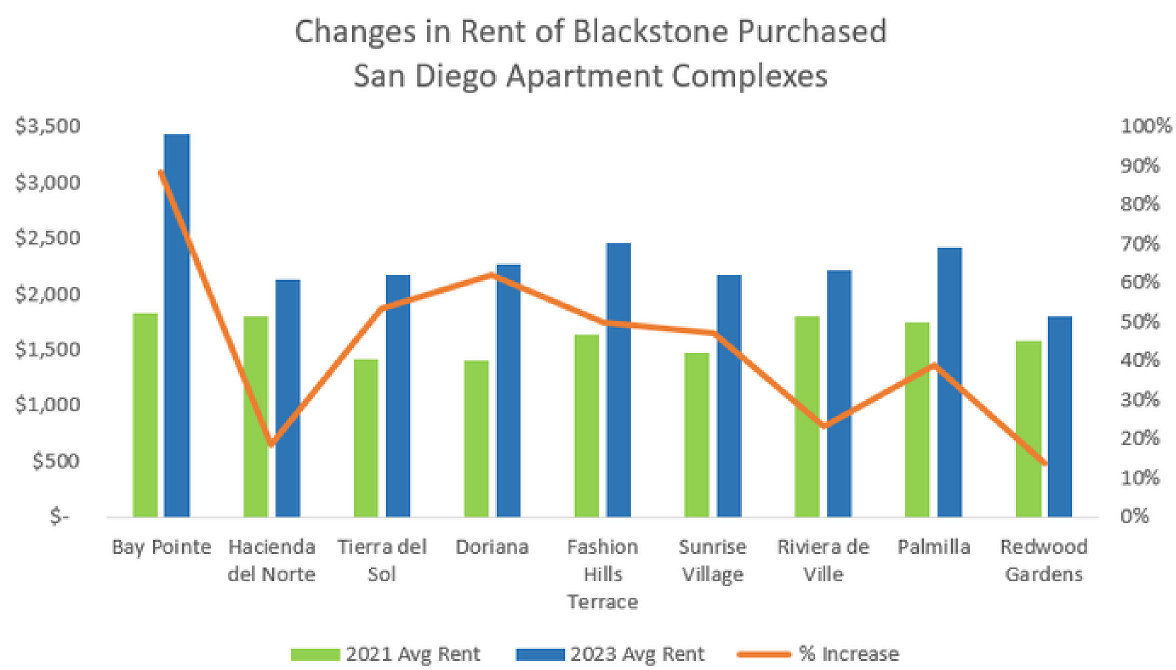


Of the state's 58 counties, San Diego has the third most at-risk homes (Los Angeles and Orange counties are first and second, respectively.) In addition to the loss of government-based subsidies, these conversions of affordable to market rate housing units are the result of restrictive covenants expiring and changes in ownership that terminate such agreements, which otherwise keep prices connected to incomes.

As an example of rates changing following a change in ownership, in August 2021, Blackstone bought 5800 mostly missing middle apartments in San Diego County. At the time they stated that they intended to keep the rentals affordable and to invest in improving the properties.

However, later that same year, a group of tenants participating in a protest claimed that Blackstone, in the midst of the pandemic and in contradiction to their earlier promises, was raising rents and failing to renovate their rundown properties.

Asking rents for new tenants at the ten largest apartment complexes now owned by Blackstone have all gone up. The chart below shows the average rent paid by tenants in 2021 (all unit sizes) and compares that average to the asking rent in 2023 for a one-bedroom apartment.

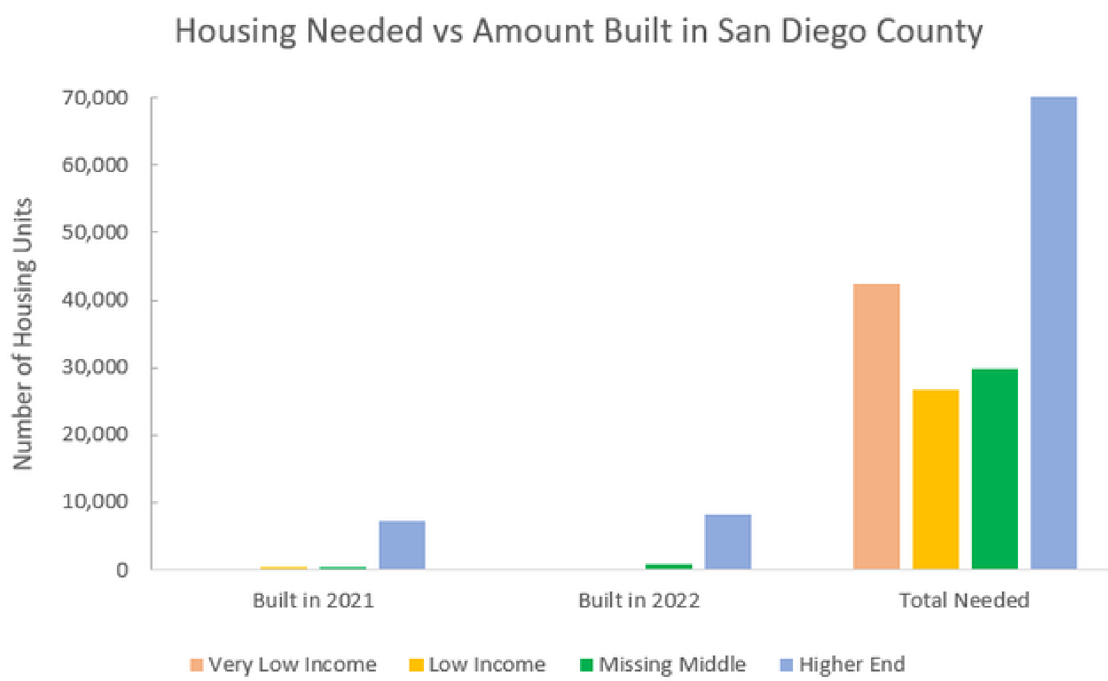


How Much is Needed?

While we need additional housing at all income levels, certain income categories are in greater demand than others. Nationwide, 96% of the housing currently being built requires an income of $75,000. While that salary might go a lot further in some parts of the country, in San Diego County that would be considered "low income" even for a single individual.

The San Diego Association of Governments recently completed a report indicating that the county needs an additional 171,685 housing units to be built between 2021 and 2029. The missing middle market itself needs 29,734 additional units during this time frame.

However, in 2021 only 456 MMH units were added, while 7237 units or 90% of the additional housing supply constructed was at the highest income level. Things were not much different in 2022 when 745 additional missing middle units were added, while 88% of the new supply came in at the highest level. This suggests that in the last two years we have only added 4% of the amount of the missing middle housing needed by 2029, whereas to be on track we should have already produced 22%.



Summary

While this paper focuses on San Diego County, the fact remains that housing for middle-income wage earners is critical to individuals as well as communities. Far too many people struggle to provide housing for themselves or their families at a price point that affords them the opportunity to save for a home, send a child to college, have health insurance, or to fully participate in life. With a concerted effort to focus on the missing middle, housing can be built that bridges the gap between affordable developments created through government subsidies and market rate developments.

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