

Detroit Inclusionary Housing Plan & Market Study

Preliminary Inclusionary Housing Feasibility Study

Executive Summary

August , 2016

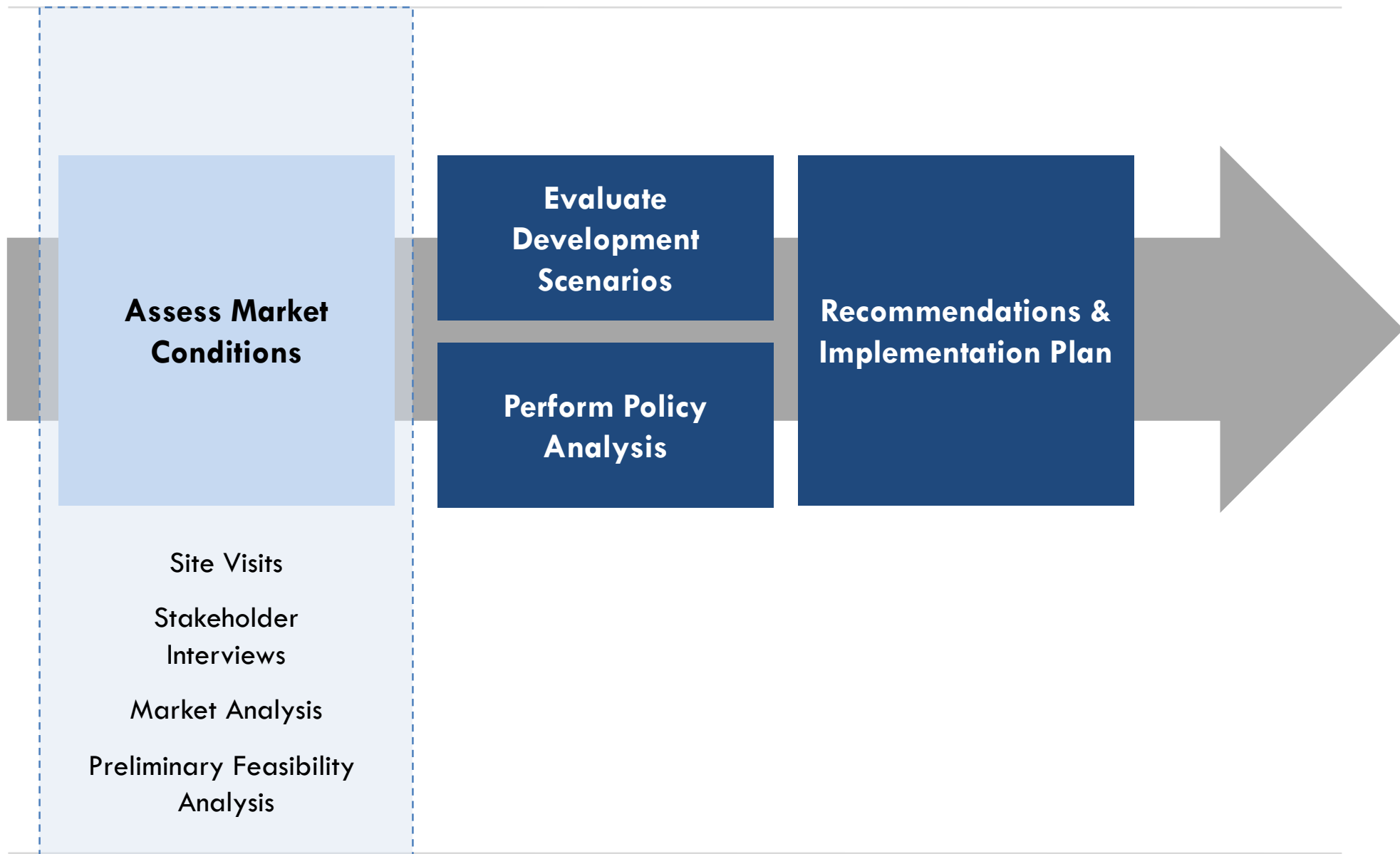
HR&A
Analyze. Advise. Act.



Inclusionary Housing Plan & Market Study Objectives

- 1** Evaluate the citywide market for multifamily housing and the potential impacts of the proposed housing ordinance.
- 2** Identify best practice tools and strategies that may guide Detroit's affordable housing strategy and inclusive growth goals.
- 3** Create a comprehensive recommendation for Detroit's affordable housing strategy, considering inclusionary housing as well as other strategies.

Inclusionary Housing Plan & Market Study Approach



Today's Focus



Multifamily market & affordable housing analysis

Development feasibility analysis

Implications for Detroit's affordable housing strategy

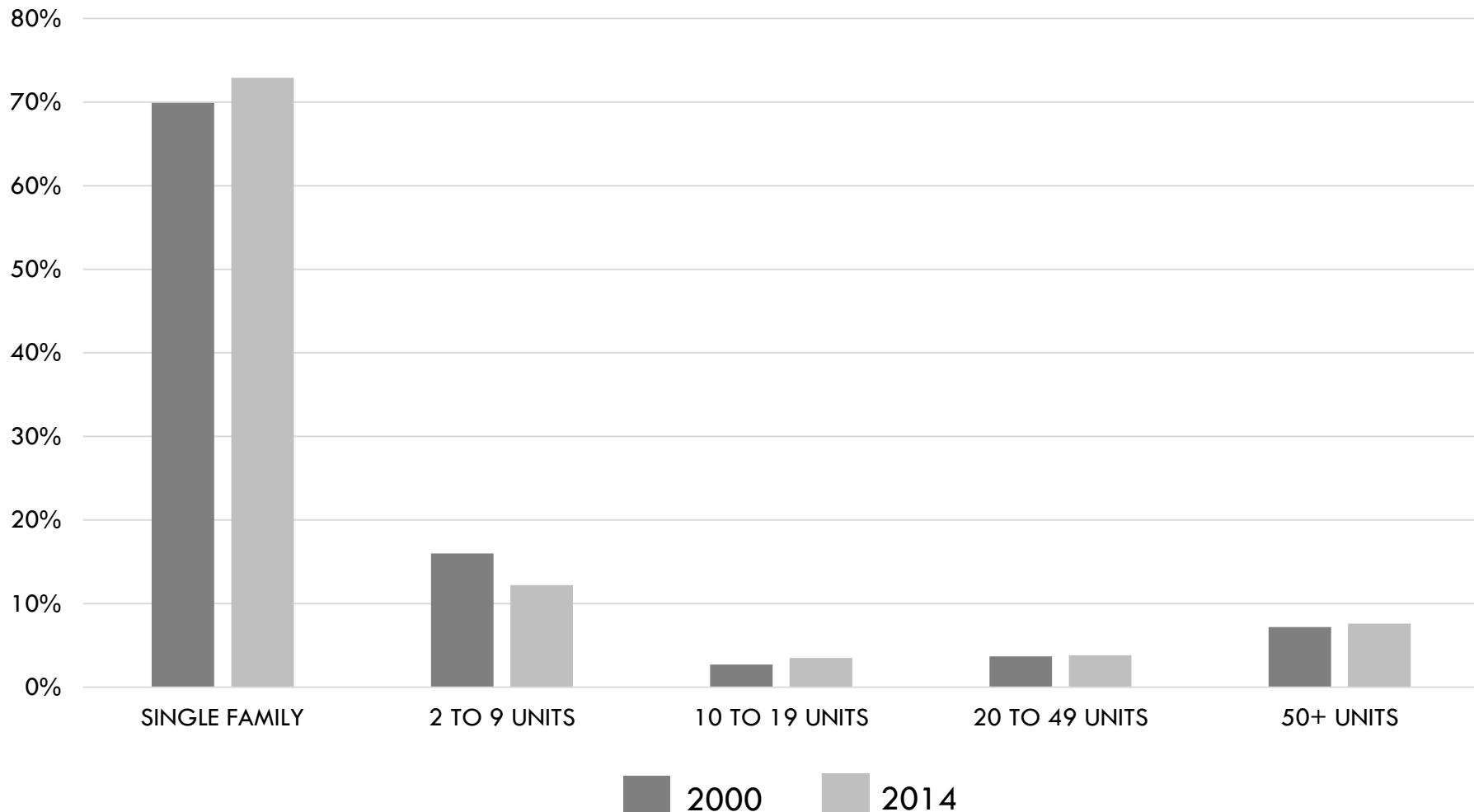
Discuss & next steps

While Detroit remains a predominantly single-family home market in terms of overall stock...



RESIDENTIAL UNITS BY UNITS IN STRUCTURE

City of Detroit
2000 & 2014

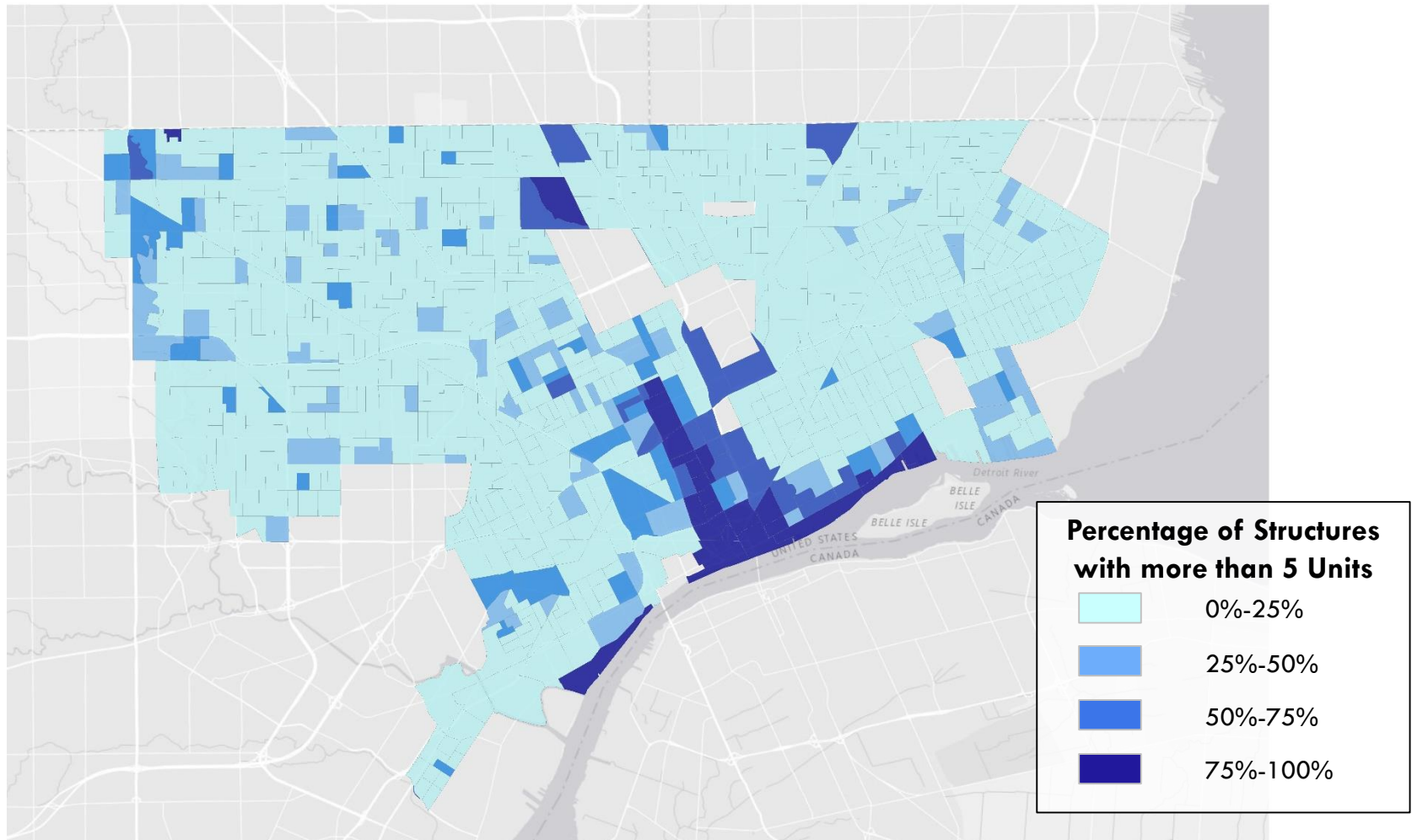


Sources: Social Explorer; HR&A Advisors

...there is a significant multifamily housing stock, of over 125,000 units, particularly concentrated in Greater Downtown.



MULTIFAMILY STOCK DISTRIBUTION City of Detroit



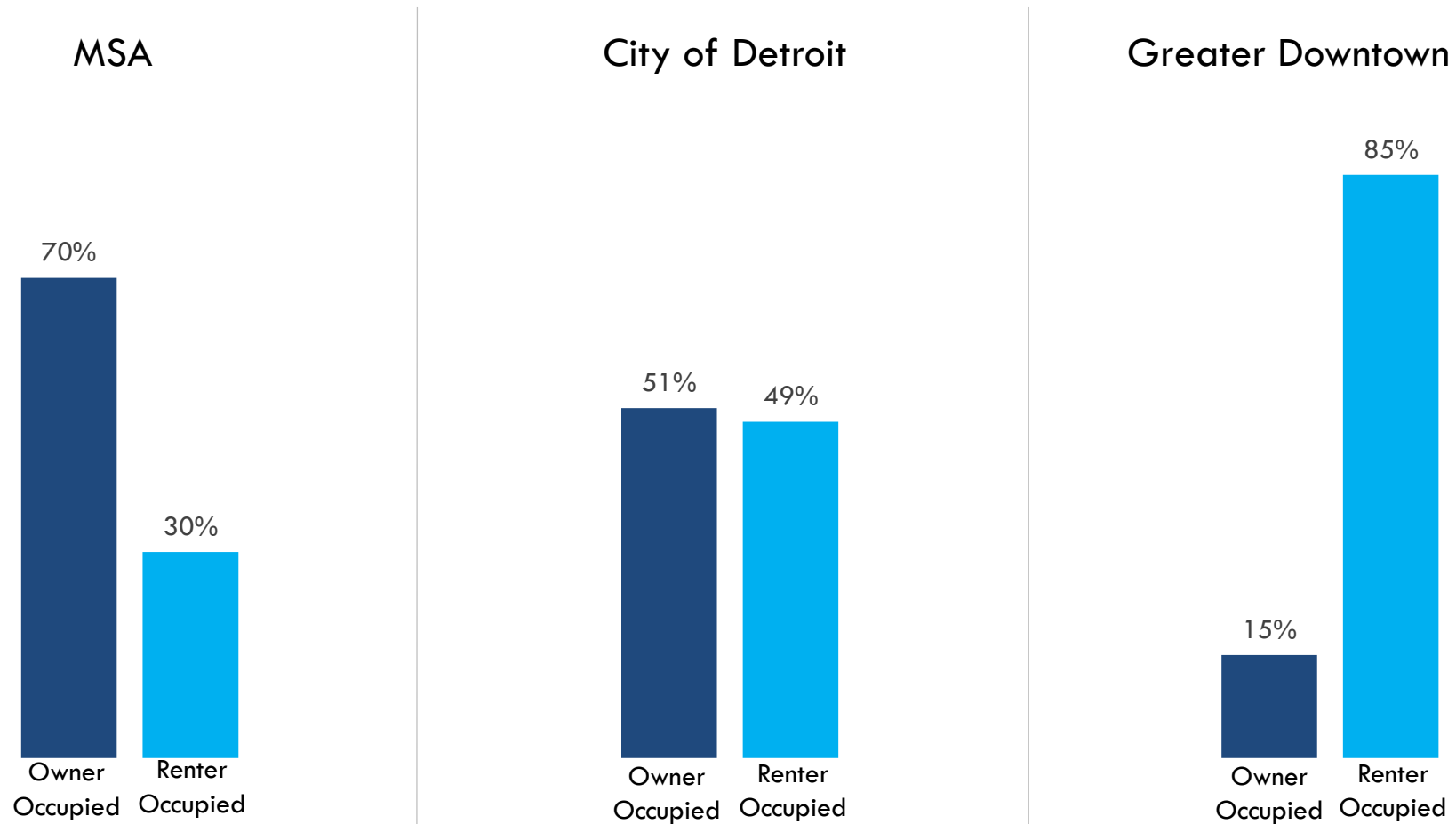
Sources: ESRI; HR&A Advisors

Tenure reflects housing stock, with a higher renter population in Detroit than the MSA, and even more concentrated in Greater Downtown.



TENURE

MSA, City of Detroit & Greater Downtown 2014

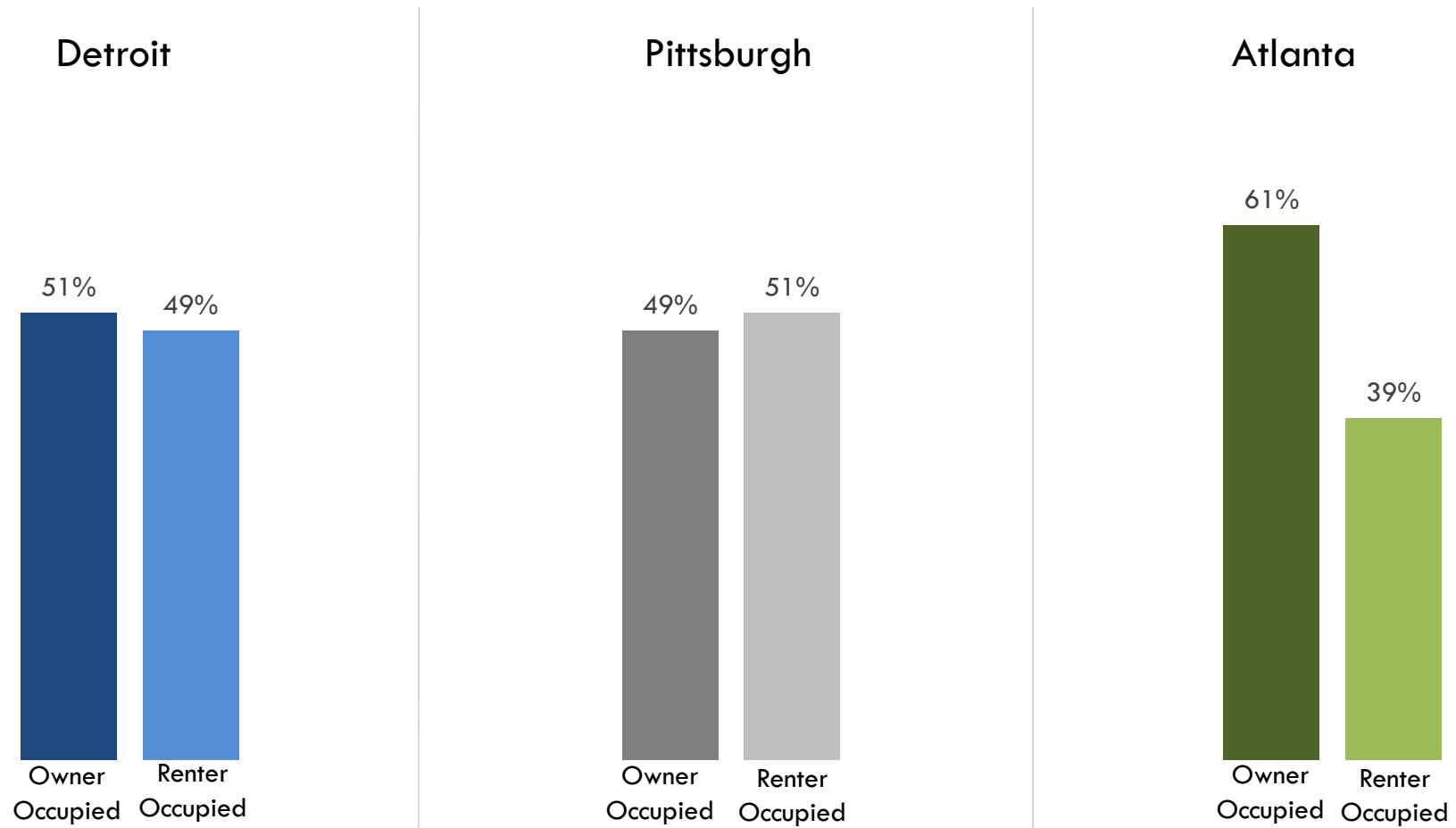


Sources: Social Explorer; HR&A Advisors

Detroit's renter vs. owner breakdown is similar to comparable American cities.



TENURE BY CITY 2014



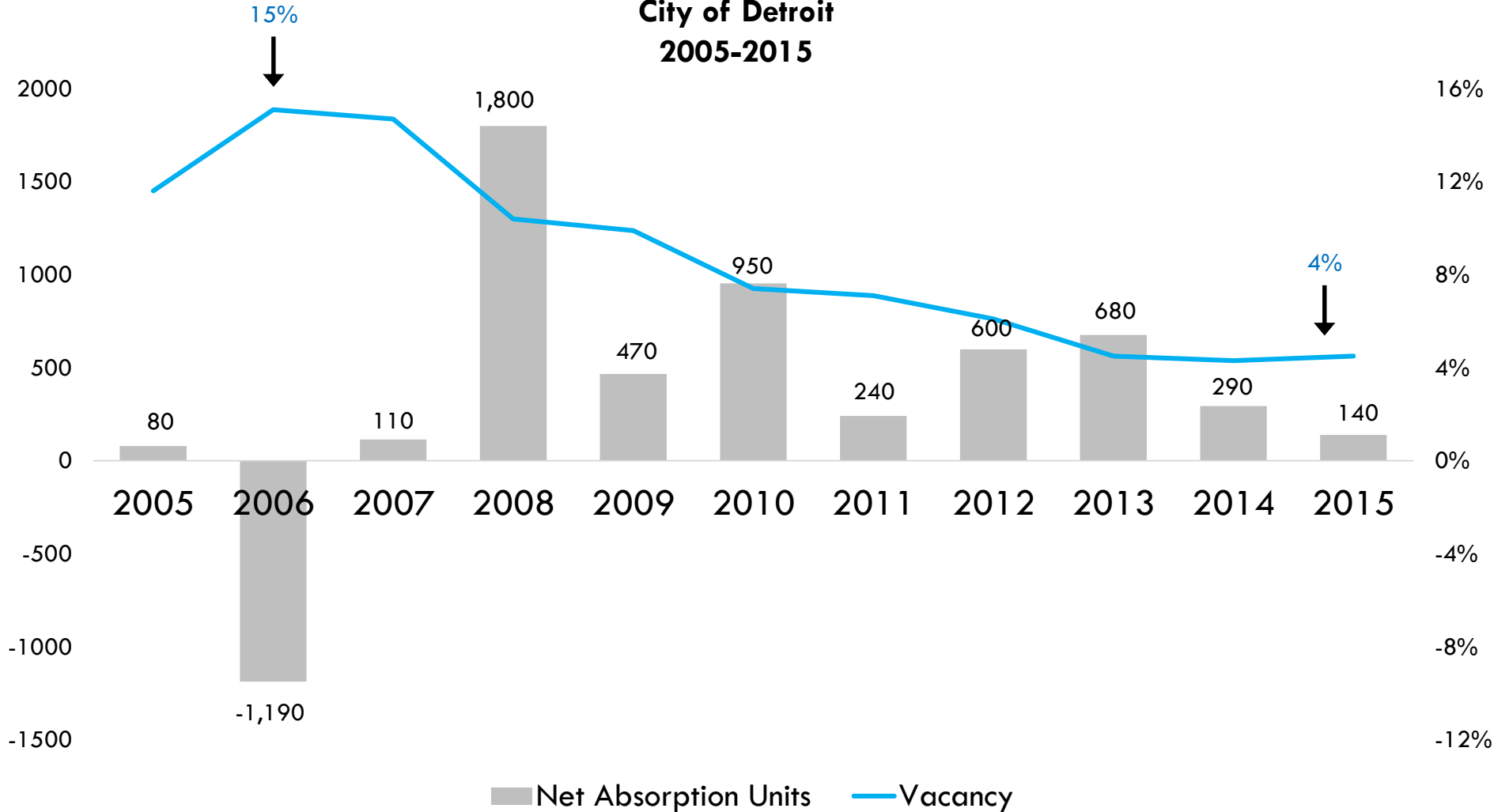
Sources: Social Explorer; HR&A Advisors

The multifamily market is evolving, showing signs of strength, including positive absorption and reduced vacancy.



MULTIFAMILY HISTORY

City of Detroit
2005-2015

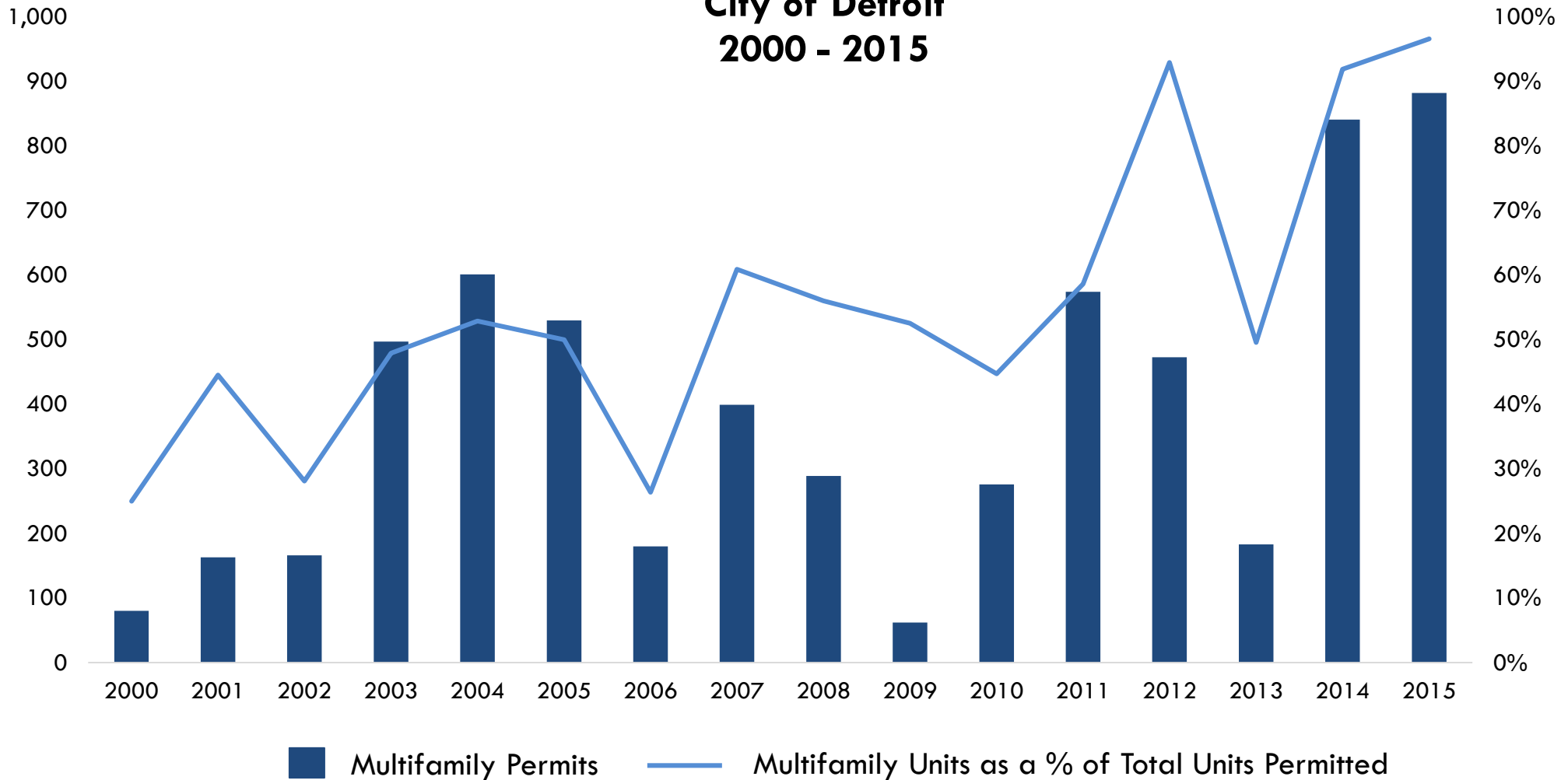


Sources: CoStar; HR&A Advisors

As of 2014, multifamily development has surpassed its pre-Recession peak.



MULTIFAMILY BUILDING PERMITS City of Detroit 2000 - 2015

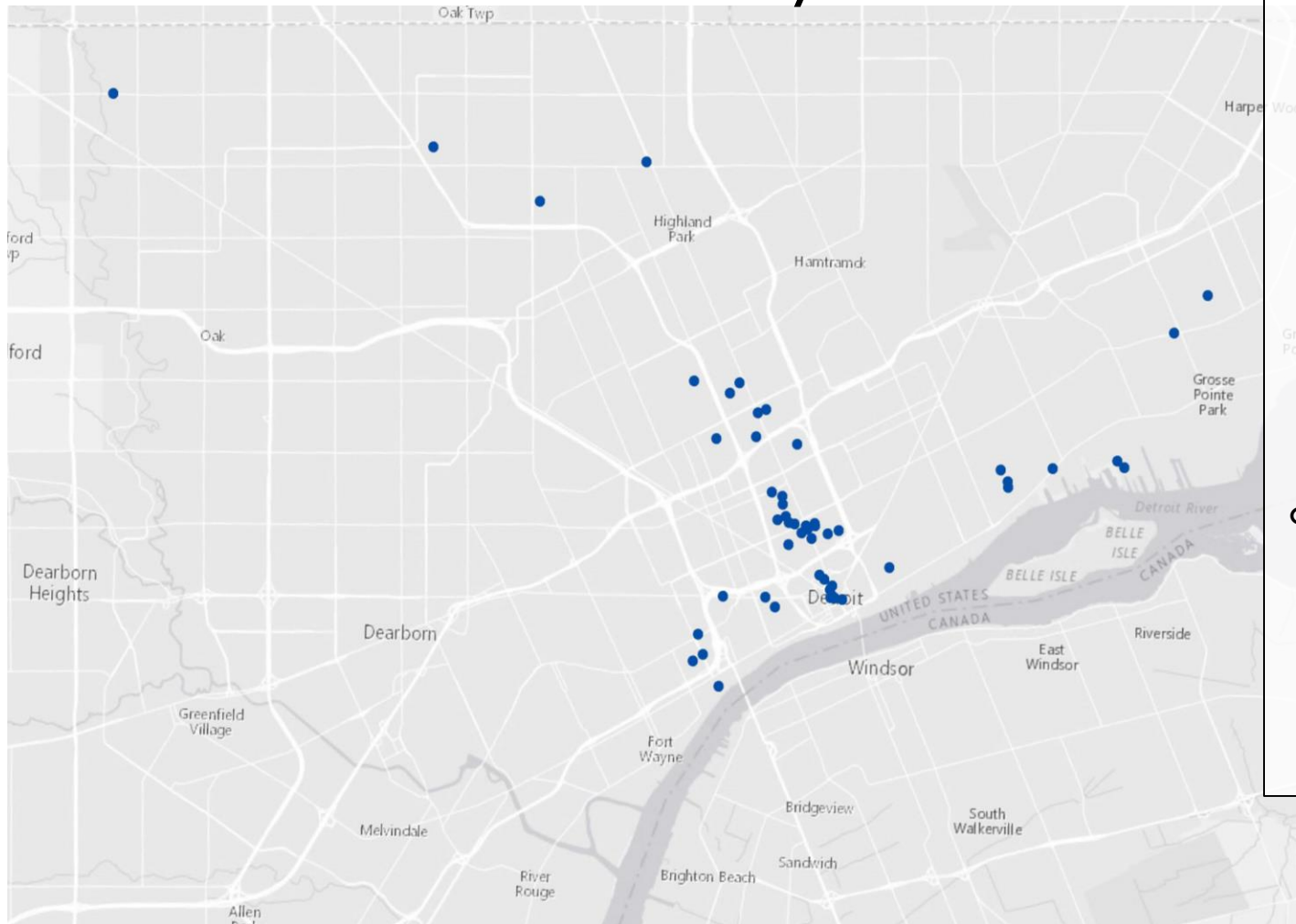


Sources: SEMCOG; HR&A Advisors

Today, Detroit's multifamily pipeline includes 56 projects under construction and in planning stages.



MULTIFAMILY PIPELINE City of Detroit



56
Pipeline projects

~4,951
Pipeline units

54%/46%
Rehab/New construction

73%
of total pipeline projects in
Greater Downtown

83%
of total pipeline units in
Greater Downtown

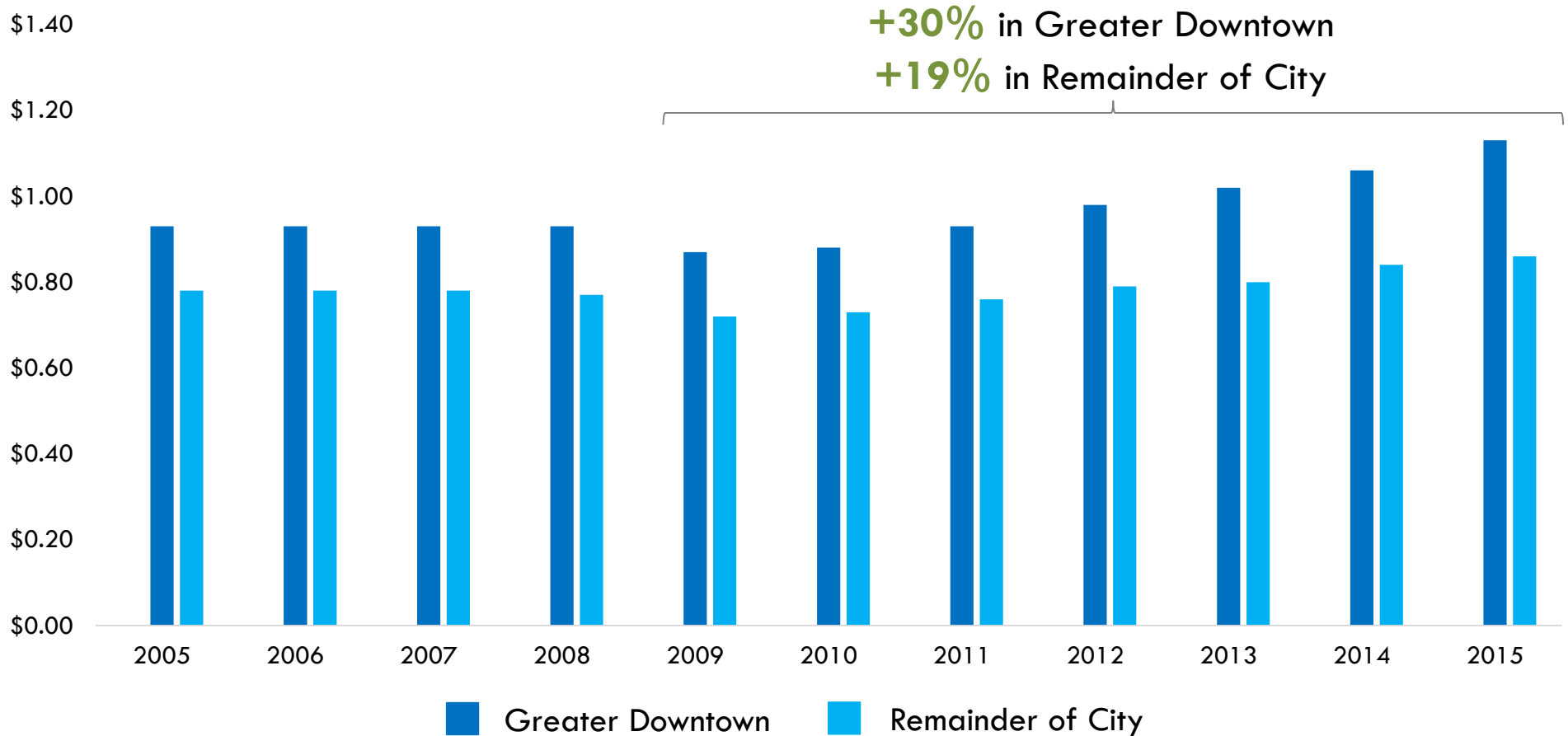
Sources: City HRD; HR&A Advisors

As new product is delivered, rents have experienced steady growth, particularly in Greater Downtown.



MULTIFAMILY RENT

City of Detroit, Greater Downtown & Remainder of City
2005 - 2015

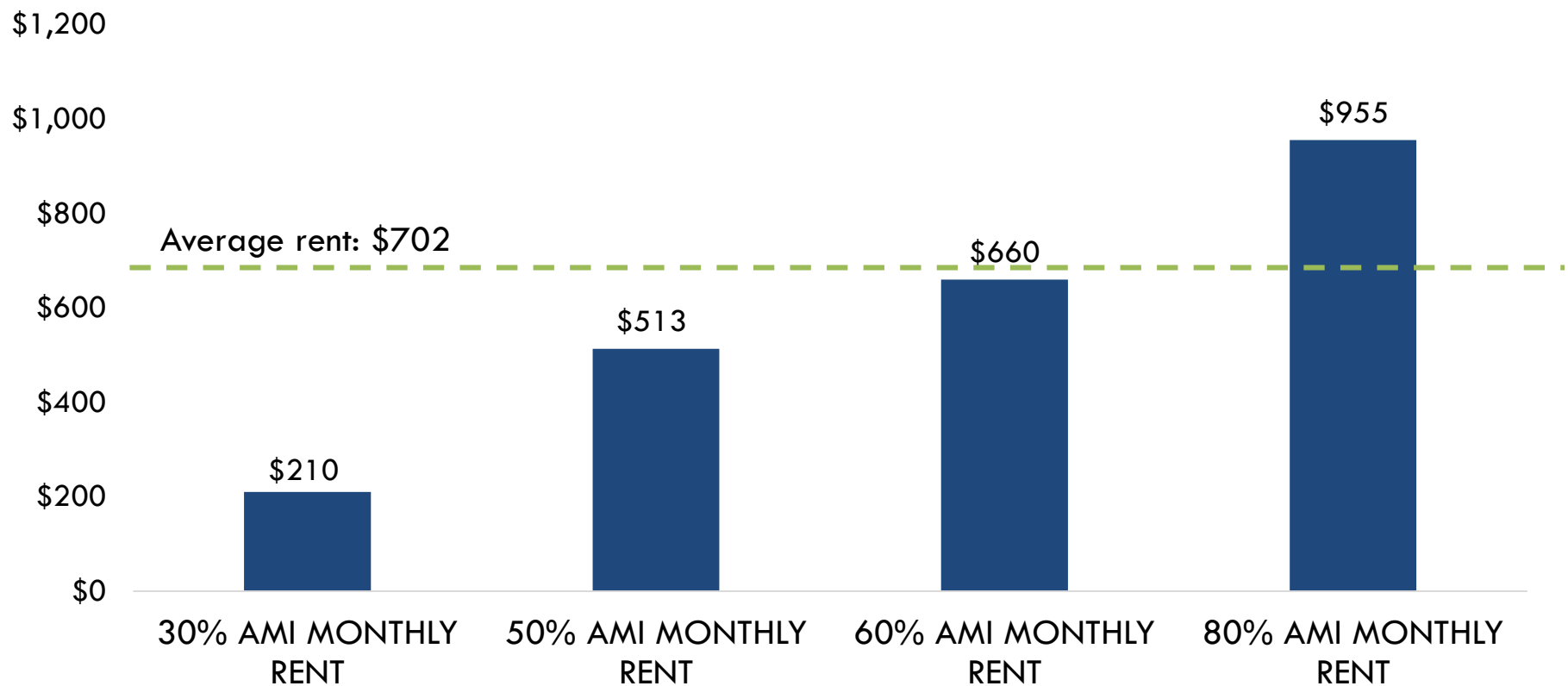


Sources: CoStar; HR&A Advisors

The average monthly rent in Detroit is affordable to households making above 60% of AMI.



MONTHLY RENT BY AFFORDABILITY LEVEL, ONE BEDROOM UNIT



Income Limit
(2 person HH):

\$16,080

\$26,800

\$32,160

\$42,880

*Note: Average rent in Detroit is based on the citywide average rent for a one bedroom unit.
Source: CoStar; Department of Housing and Urban Development; HR&A Advisors.*

While market rents across the city are low, less than one fourth of units are affordable to extremely low income households.



SHARE OF RENTAL UNITS AFFORDABLE AT AMI BENCHMARKS

City of Detroit
2014

| Unit Type | < 30% | 50% | 60% | 80% | > 100% |
|------------------------|------------|------------|------------|------------|------------|
| Studio / One Bedroom | 32% | 78% | 89% | 97% | 99% |
| Two Bedrooms | 16% | 64% | 89% | 97% | 99% |
| Three or More Bedrooms | 12% | 60% | 83% | 98% | 100% |
| All Units | 23% | 67% | 86% | 97% | 99% |

Note: "Affordable" means a household spends no more than 30% of income on housing costs (gross rent, including utilities). Per HUD guidelines, studio / one bedroom units assume a household size of two, two bedroom units assume a household size of four, and three or more bedroom units assume a household size of six.

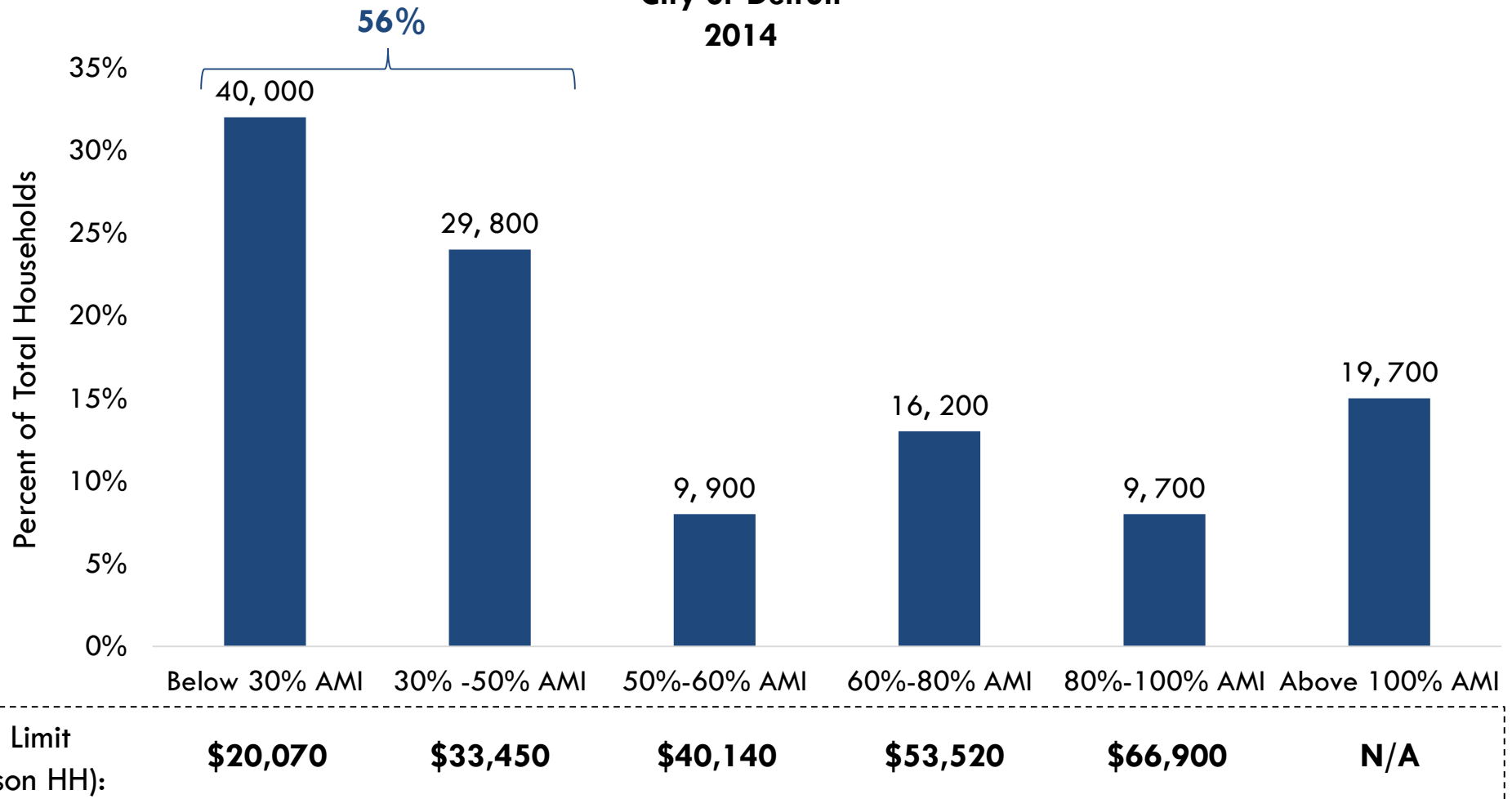
Sources: American Community Survey PUMS Data; HR&A Advisors

Over 50% of renter households make 50% or less of the MSA's AMI.



RENTER HOUSEHOLD INCOME BY AMI BENCHMARKS

City of Detroit
2014

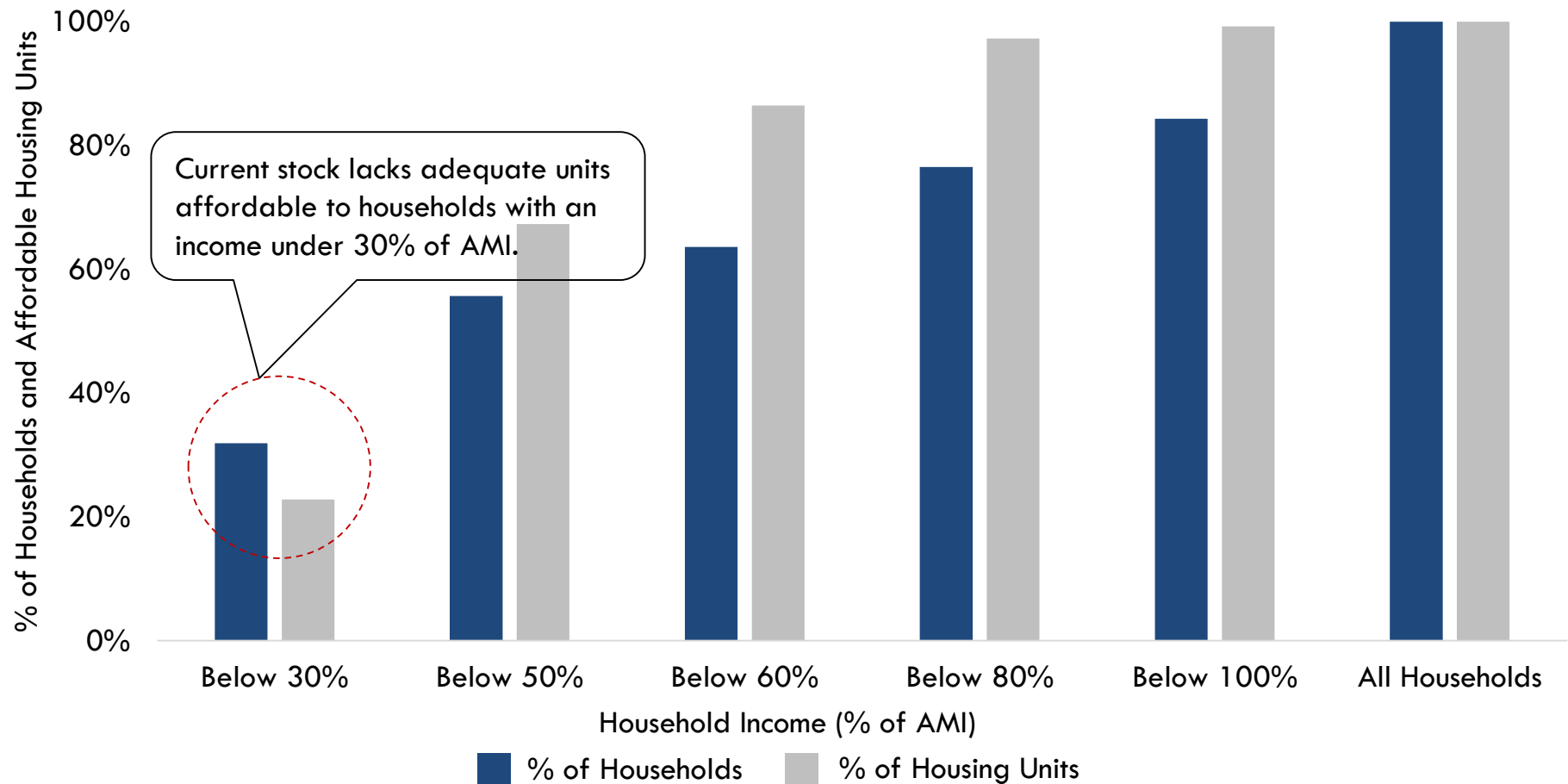


The gap between need vs. availability of affordable housing is concentrated at the lowest income bracket.



SHARE OF RENTAL UNITS AFFORDABLE TO DETROIT HOUSEHOLDS BY AMI LEVEL

City of Detroit
2014

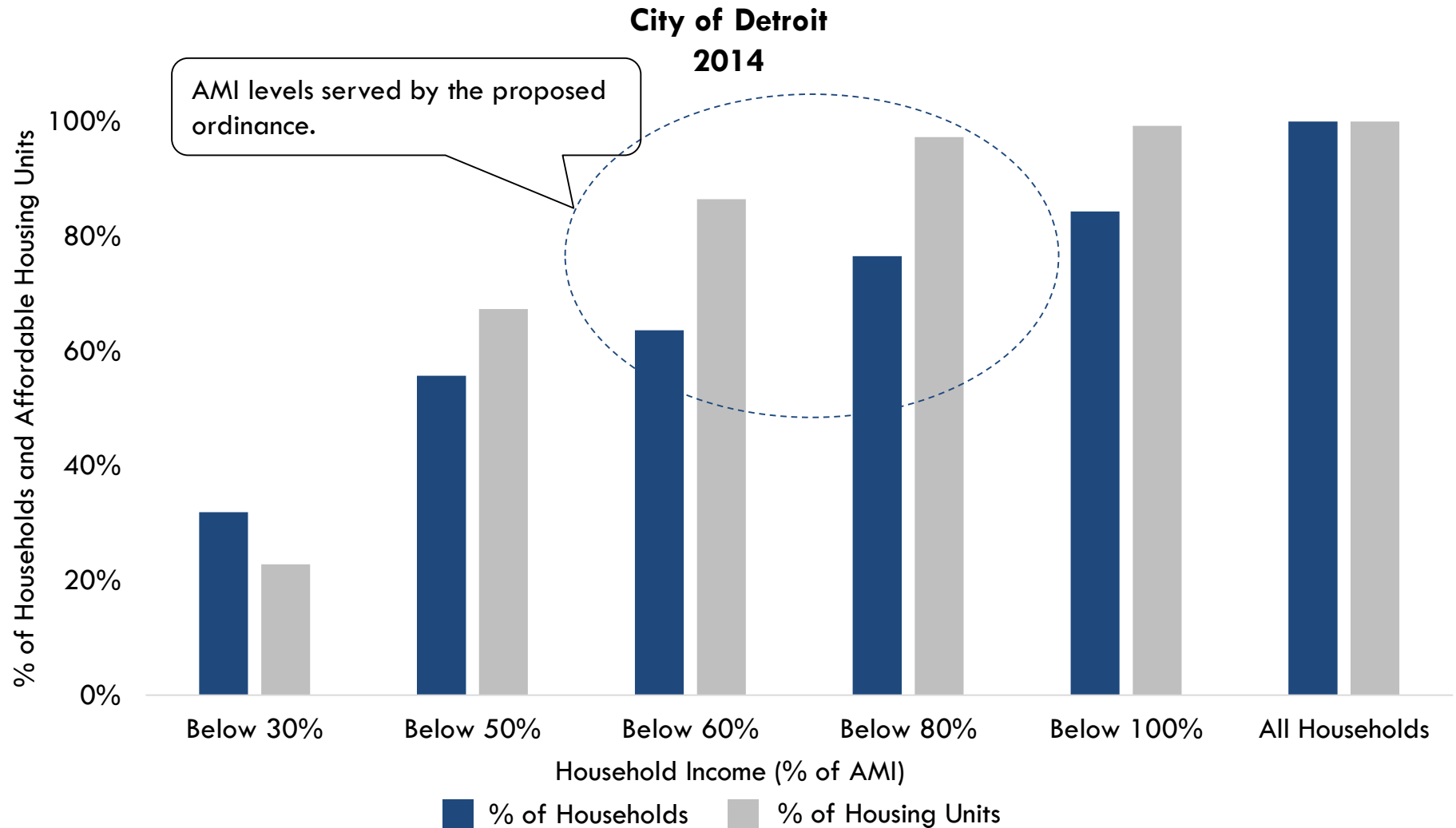


Sources: American Community Survey PUMS Data, Total rental households; HR&A Advisors

The proposed ordinance aims to create housing for households who currently have adequate housing supply.



SHARE OF RENTAL UNITS AFFORDABLE TO DETROIT HOUSEHOLDS BY AMI LEVEL

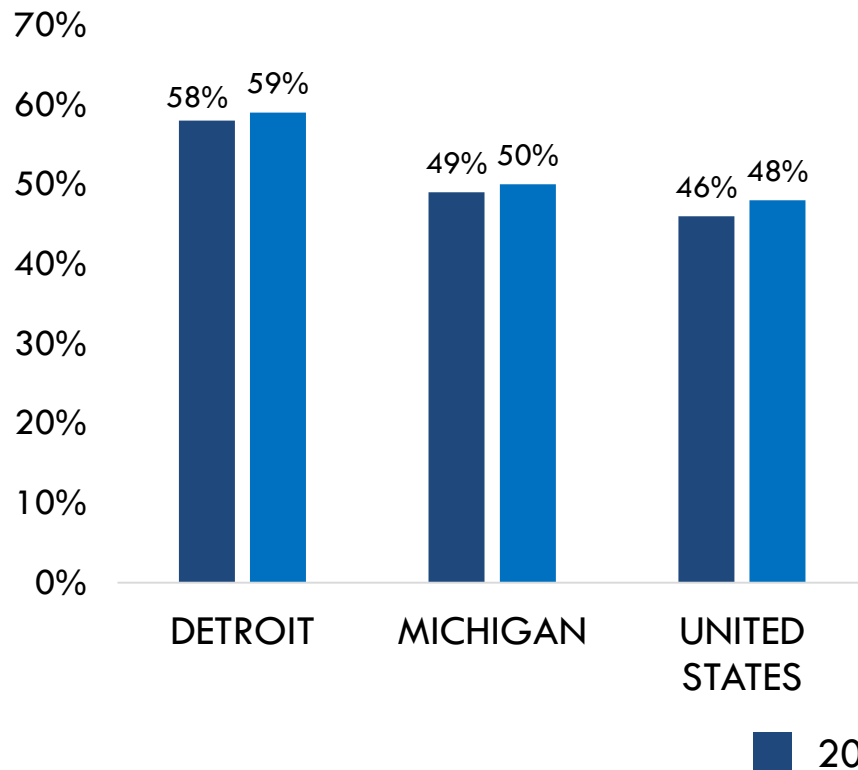


Sources: American Community Survey PUMS Data, Total rental households; HR&A Advisors

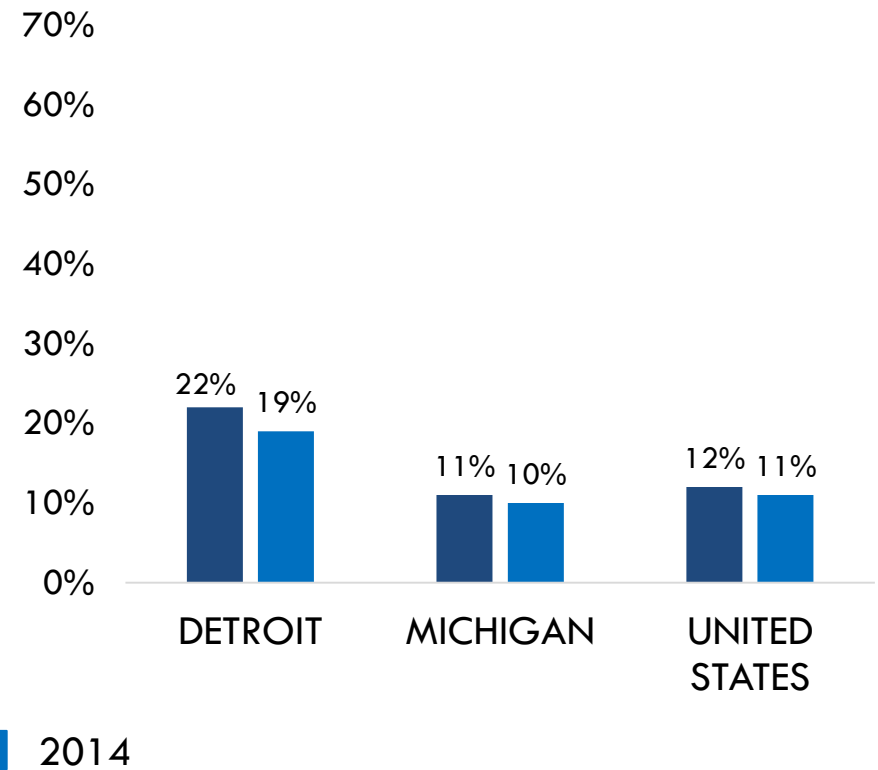
A significant portion of renters are rent burdened, spending more than 30% of their household income on housing costs.



RENT-BURDENED HOUSEHOLDS (> 30% Of Income Toward Housing Costs) City of Detroit, Michigan & United States 2009 & 2014



EXTREMELY RENT-BURDENED HOUSEHOLDS (> 50% Of Income Toward Housing Costs) City of Detroit, Michigan & United States 2009 & 2014









Note: Rent burdened households are defined as spending more than 30% of income on housing costs (gross rent, including utilities). Extremely rent burdened households are defined as spending more than 50% of income on housing costs (gross rent, including utilities).

Sources: Policy Map; American Community Survey PUMS Data; HR&A Advisors

A range of affordable housing programs can be used to preserve or produce affordable housing for specific populations.



FEDERAL AFFORDABLE HOUSING PROGRAMS & TARGET POPULATIONS

| Federal Program | Target Population (Household AMI) |
|--|--------------------------------------|
|  Community Development Block Grants | Less than 80% of AMI |
|  Housing Opportunities for Persons with AIDS | Less than 80% of AMI |
|  HOME Investment Partnership Program | Less than 80% of AMI |
|  Low Income Housing Tax Credits | Less than 60% of AMI |
|  Housing Choice Vouchers (Section 8) & Project Based Vouchers & ACC | Less than 30% of AMI |
|  Emergency Solutions Grant (ESG) | "Homeless" individuals |

Detroit has created opportunities for the residential market, though still faces challenges in supporting development and particularly affordable housing.



SIGNS OF GROWTH

As presented above:

- High occupancy rates in new multifamily developments in strong submarkets.
- Increasing rents and continued demand for new multifamily units in the Greater Downtown area.
- An influx of investment, including new retail and amenities, around residential product in downtown neighborhoods.

CONTINUED CHALLENGES

To be discussed below:

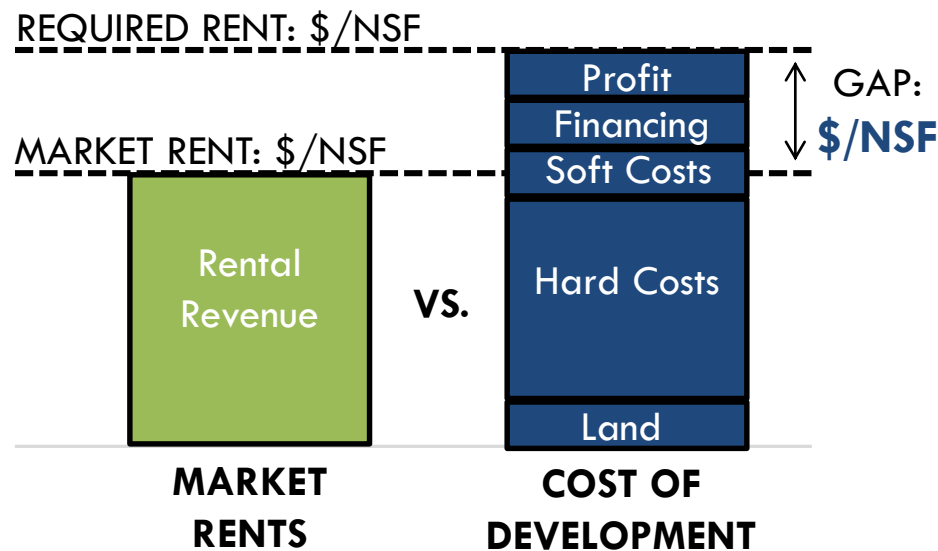
- Infeasibility of market rate development, particularly in neighborhoods outside of Greater Downtown.
- A burdensome property tax rate that requires abatements to make development possible.
- An unpredictable, complex development approvals process that discourages potential developer interest in Detroit.

To measure development feasibility the impact of affordability requirements, the team analyzed rents required.



Typically, the costs associated with an inclusionary policy impact land value. The residual land value of a property to a developer decreases due to the reduced potential rental revenue of projects with an inclusionary requirement.

However, rents in Detroit are too low to fully absorb the impact of a mandatory inclusionary housing policy under current market conditions. Even after reducing land costs to \$0, a gap persists across all neighborhood typologies, triggering a need for additional public support, which increases project complexity and may weaken developer interest or project feasibility. The following analysis illustrates the required rents needed to support development.



HR&A did not model condos given the lack of a market for condos and lack of applicable subsidies to facilitate development. Rents calculated for net square footage (NSF), assuming a 15% loss factor from gross square footage (GSF).

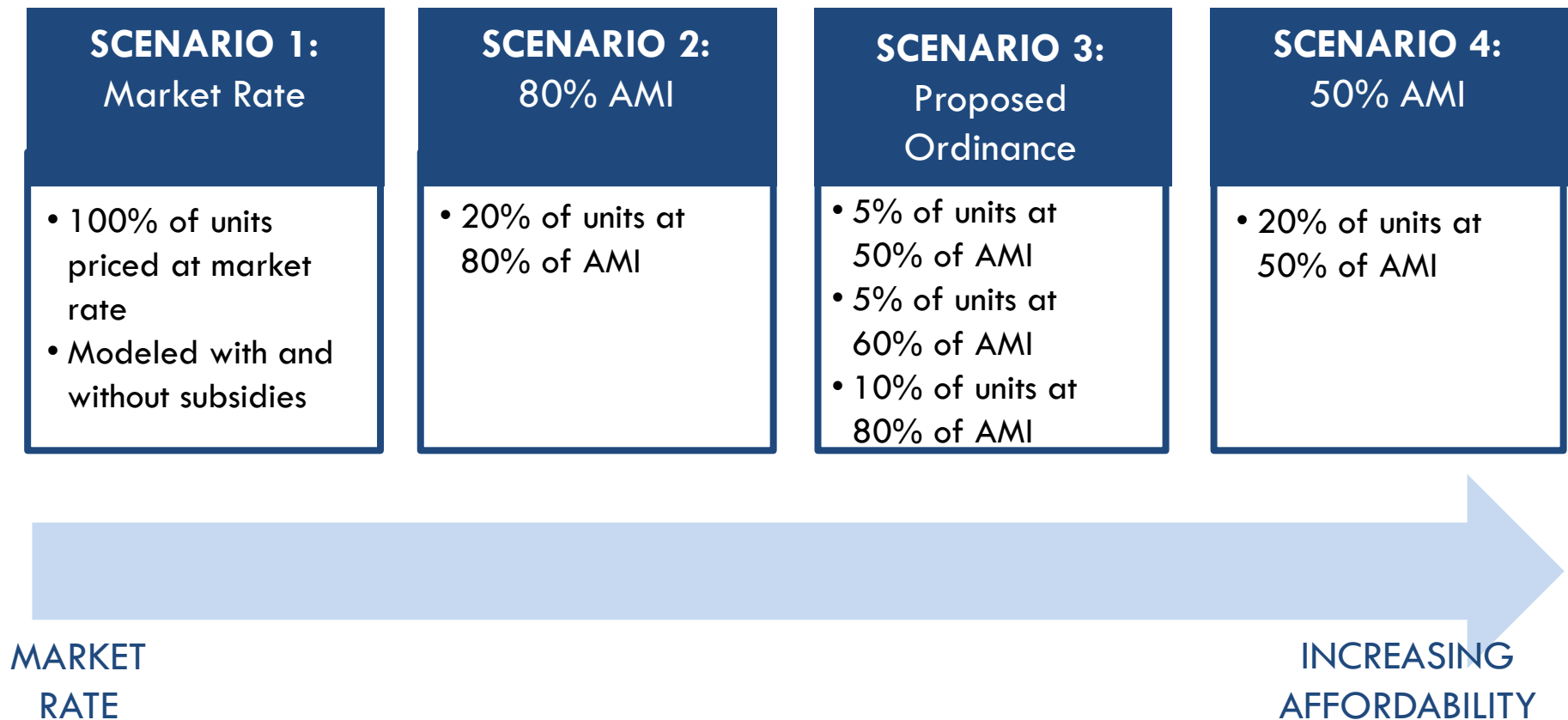
Market assumptions vary across the City and are highly dependent on conditions at the neighborhood level.



| Metric | Typology One: Greater Downtown | Typology Two: Active Commercial Corridors | Typology Three: Partially Active Commercial Corridors | Typology Four: Mostly Inactive Commercial Corridors |
|--|--------------------------------------|---|--|--|
| Market Rate Rent /SF/Month | \$2.00 | \$1.40 | \$1.15 | \$0.90 |
| Construction Cost – New Construction | ←————— \$190/GSF —————→ | | —————→ | |
| Construction Cost – Historic Rehabilitation | ←————— \$205/GSF —————→ | | —————→ | |
| Land Value per GSF | \$10 | \$8 | \$5 | \$3 |
| Cap Rate | 7.25% | 8.0% | 8.5% | 9.0% |

Construction costs include hard cost plus 20% soft costs.

The team analyzed four levels of affordability for both new construction and reuse.



Where development without public support was infeasible, HR&A included the benefit of frequently-used tools to model feasibility.



This preliminary analysis considers the use of tax abatements and historic tax credits, where applicable. Future analysis will examine additional tools for funding and financing development requiring support to reach feasibility.

Tax abatements are currently a critical source of public support for most new development in Detroit given elevated tax rates in the City. The current property tax rate for apartment buildings in Detroit is 84.8 mills, which translates to an effective tax rate of approximately 4.2%. Apartment property taxes in Detroit rank second highest among large cities nationwide.

PUBLIC SUPPORT PACKAGE MODELED BY PRODUCT TYPE

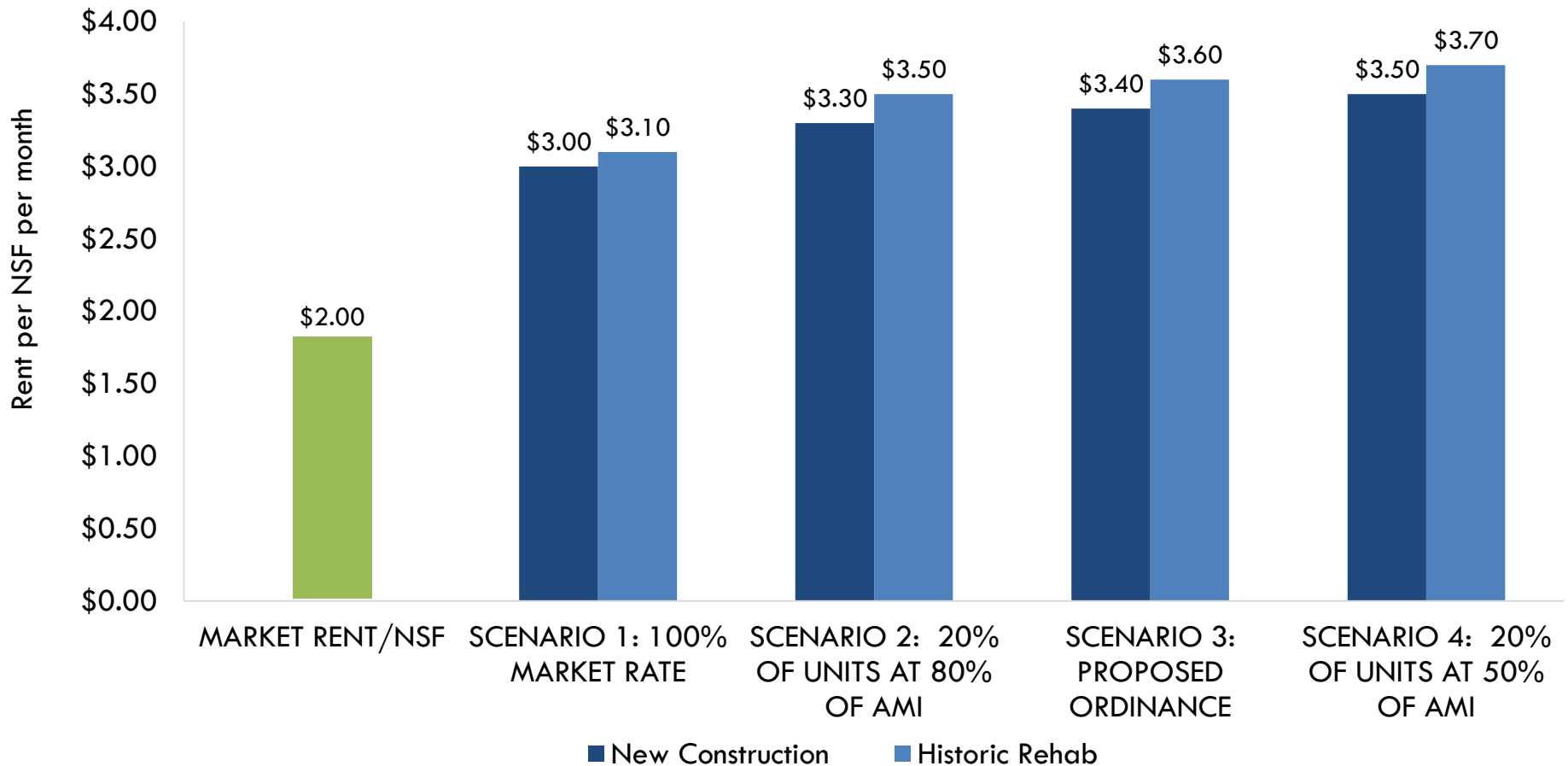
| | |
|--|---|
| Low to Mid-Rise New Construction | Historic Rehab |
| <ul style="list-style-type: none">• Tax Abatements | <ul style="list-style-type: none">• Tax Abatements• Federal Historic Tax Credits |

While Greater Downtown commands the highest multifamily residential rents in Detroit, a rent gap persists.



NEIGHBORHOOD TYPE 1: GREATER DOWNTOWN, NO PUBLIC SUPPORT

Required rents would need to increase 50-55% to support development without additional public support at market rate. Layering in the proposed ordinance raises this gap to 70-80%.

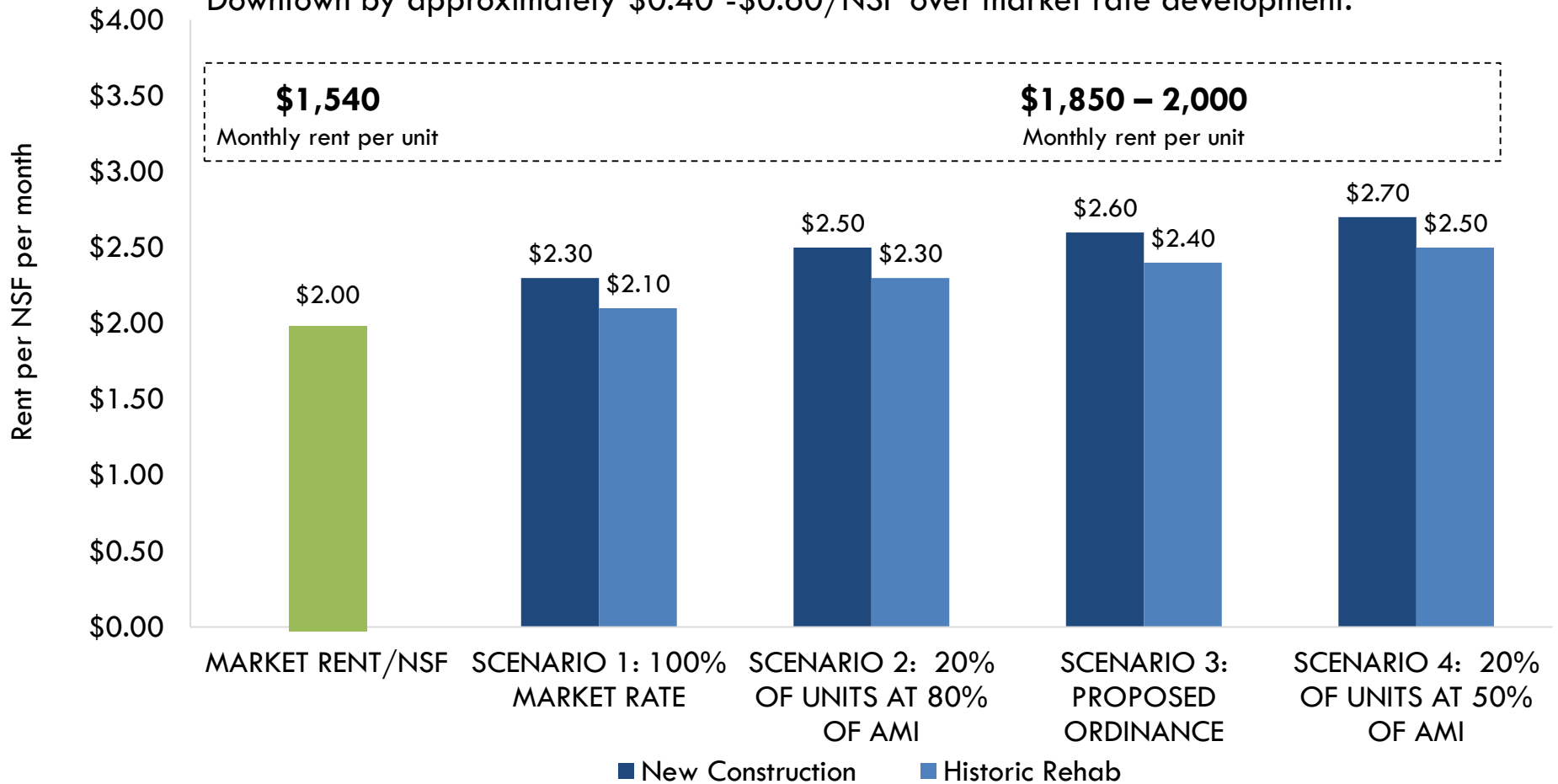


Commonly-available subsidies nearly, but do not completely, close the feasibility gap in Detroit's strongest market.



NEIGHBORHOOD TYPE 1: GREATER DOWNTOWN, WITH STANDARD PUBLIC SUPPORT

With public support, the proposed ordinance would increase required rents in Greater Downtown by approximately \$0.40 - \$0.60/NSF over market rate development.



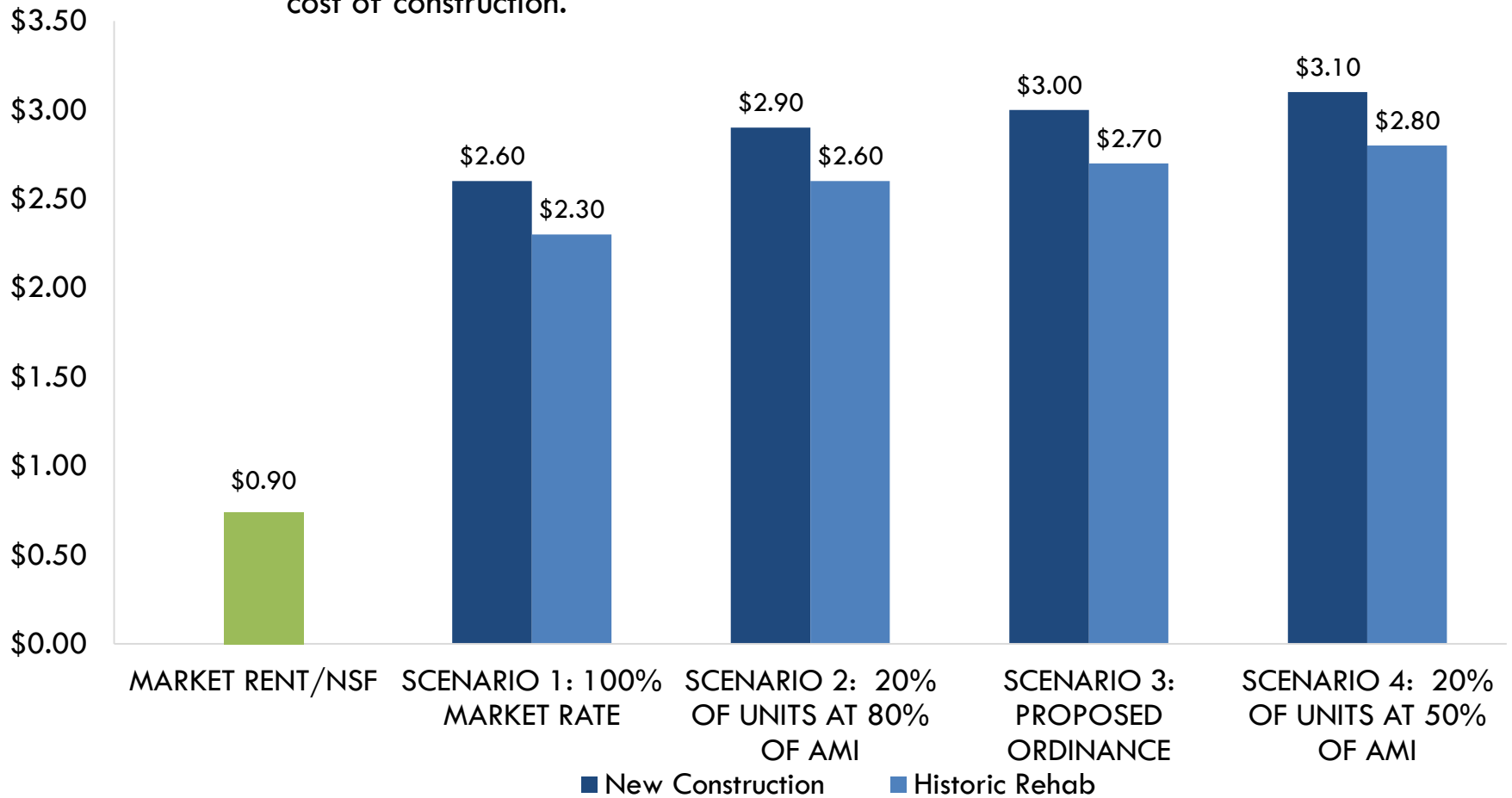
Subsidies modeled include tax abatements for new construction projects and tax abatements and historic tax credits for historic rehab projects. Tax abatements assume property taxes are frozen at the predevelopment value. Historic tax credits assume a 20% credit on qualified rehab expenditures.

Mostly inactive commercial corridors face the largest rent gap and cannot support new development without significant public support.



NEIGHBORHOOD TYPE 4: MOSTLY INACTIVE COMMERCIAL CORRIDOR, WITH

PUBLIC SUPPORT. Required rents rise in weaker submarkets due to low market confidence and cost of construction.



Subsidies modeled include tax abatements for new construction projects and tax abatements and historic tax credits for historic rehab projects. Tax abatements assume property taxes are frozen at the predevelopment value. Historic tax credits assume a 20% credit on qualified rehab expenditures.

Analysis indicates that the proposed Inclusionary Housing ordinance may not be the most effective tool for Detroit.



The proposed ordinance does not address the portion of Detroit's population with the greatest affordable housing need: households earning less than 30% AMI. It is designed to help prevent displacement of households earning less than 50% and 80% AMI if rents continue to rise.

Given low land values as a product of current market conditions, the proposed inclusionary zoning policy is not economically viable. For this policy to be successful, there needs to be sufficient project profitability or land value to support cross-subsidization. Today, even the city's strongest markets require subsidy to support market rate development's feasibility.

Variation in market conditions across the City requires carefully targeted policies that respond to individual neighborhood market characteristics. As Detroit's market continues to grow, the most effective strategies for affordable housing will evolve. Today, the City should consider strategies that preserve existing affordable housing and support those in the greatest need, while planning for policies that respond to future market conditions (including inclusionary housing).

Analysis reveals Detroit's most pressing affordable housing needs and suggests a direction for future recommendations.



Extremely low-income and very low income households are in the greatest need of affordable housing in Detroit. Affordable housing policies that preserve or create new units for these income brackets are critical for near-term consideration.

Development in Greater Downtown, a relatively strong submarket, still requires subsidy. The HR&A team will study affordable housing tools that can be brought into effect when land values rise to support the additional cost associated with affordable housing.

In other areas of the city, multifamily development would require deep subsidies. Exploring strategies to create or preserve affordable housing in other types of housing will be key as the City leads neighborhood planning initiatives.

The HR&A team is studying best practices to preserve and promote affordable housing in weak markets to guide recommendations for Detroit. A review of best practices and innovative affordable housing delivery models will provide context to frame recommendations appropriate for Detroit.

Alternative strategies may more effectively address Detroit's affordable housing needs than the proposed ordinance.



GOAL 1: Serve Detroit households most in need of affordable housing.

Example strategy: Secure operating subsidies (ACC vouchers) to maintain affordable housing.

Applicability: Households earning less than 30% of AMI cannot afford rent sufficient to cover the cost to develop and maintain housing, so programs providing operating subsidies will be critical.

GOAL 2: Encourage mixed-income development without deterring recent overall development activity.

Example strategy: Tie affordability requirements to automatic approvals to save developers time and money.

Applicability: Strong, given developer feedback around the time and cost required to complete existing development approvals process.

GOAL 3: Protect Detroit's naturally affordable and regulated housing.

Example strategy: Create an acquisition loan fund to facilitate purchase and renovations of existing properties to create or preserve affordable units.

Applicability: Strong, given the potential to preserve at-risk affordable units through maintenance or renovation.

Next Steps

