2016 CITY OF MADISON

HOUSING REPORT

MARKET RATE OWNERSHIP

TABLE OF CONTENTS

MARKET RATE OWNERSHIP - PRIORITIES

For market rate ownership housing, the primary goal is to ensure that there is sufficient quantity and diversity of supply to meet the demands of a growing population and allow a new generation of homebuyers to enter our market who have demonstrated a strong desire for housing in a location proximate to amenities and convenient transportation. When possible, efforts to provide this housing should strive to meet broader goals of strengthening neighborhoods by mixing incomes, improving aging housing stock, and adding neighborhood amenities. To achieve these goals, this report identifies two main priorities:

1. Create programs to make our existing reasonably priced neighborhoods more attractive to first-time and middle income homebuyers
    a. Identify and create a designation for Opportunity Neighborhoods that are based on factors such as:
        i. Aging housing stock
        ii. Average property value below the City average
        iii. Flat or declining property values
        iv. Located outside of the city center
        v. Longer than average days on market
    b. Encourage the development of mixed-use nodes along transit corridors in Opportunity Neighborhoods to bring amenities (restaurants, retail, civic uses) to the neighborhood to increase its desirability
        i. Create new TIF districts to support development
        ii. May require rezoning and demolition of existing single family homes
        iii. Create a pilot neighborhood program to test strategies
    c. Create a "Residential Facade Grant Program" targeting houses on high traffic residential streets in Opportunity Neighborhoods based on the City's successful Business Façade Grant Program
        i. Identify high priority corridors
        ii. Fund small matching grants or loans repaid by special assessment (~$5,000) to support exterior upgrades
        iii. Potentially funded by TIF
    d. Modify existing homeownership loan programs to drive first-time and middle income homebuyers into Opportunity Neighborhoods
        i. Increase loan limits and/or reduce interest rates for homes located within Opportunity Neighborhoods
        ii. Raise income requirements to 120% of AMI within Opportunity Neighborhoods
        iii. Rebrand and market programs through advertising and outreach
2. Support the creation of new owner occupied housing developments in urban, walkable, and amenity rich neighborhoods through middle scale/density development priced between $200,000 and $300,000
    a. Remove regulatory barriers in zoning, demolition, and subdivision rules restricting middle scale/density housing types (condominiums, town houses, small lots)
        i. Create staff team to identify code and process challenges
        ii. Research national models and best practices
        iii. Create a set of recommended code and process solutions
    b. Identify appropriate areas for middle scale development
        i. Target Neighborhoods
        ii. Target Sites
    c. Facilitate the development of new entry level owner occupied middle scale/density housing
        i. Recruit developers familiar with these product types
        ii. Encourage developers to create middle scale housing on parcels too small to support larger multifamily development or to transition from commercial development to single family neighborhoods
        iii. Support developments through TIF

OVERSIGHT AND IMPLEMENTATION RESPONSIBILITIES

	1a	1b	1c	1d	2a	2b	2c
Common Council	X	X	X	X			
Community Development	X		X	X			
Economic Development	X	X					X
Planning	X	X			X	X	X

MARKET RATE OWNERSHIP - OVERVIEW

In the past 20 years homeownership has been a rollercoaster ride of boom and bust, leaving us with a homeownership market that looks dramatically different today than 5, 10 or 15 years ago. For Millennials (18-35 years old), our next generation of homeowners, there is a historically large chance that they are living with their parents, and if not, they are renting with only 29% percent owning a home. Among those that are renting, 56% are housing cost burdened meaning that housing eats up around a third or more of their income making saving for a down payment nearly impossible.

By many measures, a significant portion of renters in our market could afford to own a home. Not just the mortgage, but the full range of responsibilities involved with homeownership from property taxes to home insurance. Given this fact, we would expect to see more of them buying homes yet young renters do not appear to be transitioning into homeownership at the rate they could be. Either renters are opting out of the American Dream or it remains out of reach for reasons beyond simple affordability.

The most likely financial hurdle facing these potential buyers is the difficulty in obtaining a mortgage despite their relatively high incomes. As previously mentioned high rents make saving for a down payment difficult. Similarly, the historically large amount of student debt held by Millennials makes it difficult to save while at the same time challenging their credit scores. These challenges are multiplied by the tightened credit market that sets a much higher bar for credit worthiness, putting homeownership out of reach for young renters who have yet to firmly establish their credit. Another factor muddying the water for would-be homeowners is competition from existing homeowners who have significant downpayments and established credit histories.

Once a household decides to choose ownership over rental, the issue of where to purchase becomes relevant. The classic way to understand this decision is that households self sort into neighborhoods that have the best combination of housing and amenities that they can afford. The data indicate that the next generation is putting a greater emphasis on the amenity side of the equation than previous generations of buyers. However in these more urban/walkable central neighborhoods with more amenities, our housing stock is often priced out of reach for these first time homebuyers and redeveloping them to add moderately priced entry level ownership products is limited by zoning, demolition, and subdivision rules that can hinder middle sized development as well as a lending market that discourages alternative ownership structures such as condominiums and cooperatives.

As a city, we have a vested interest in ensuring that the thousands of renters that we have added in recent years have an option to stay in our community if and when they choose to become homeowners.

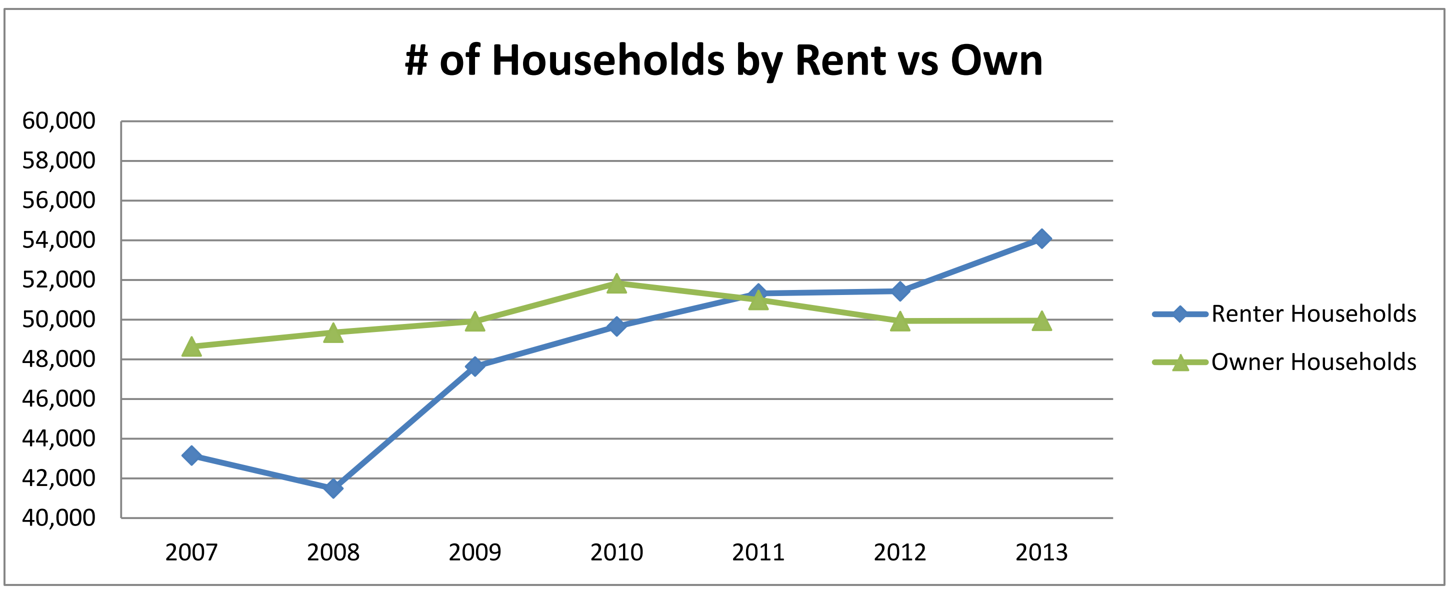
MARKET RATE OWNERSHIP - DEMAND

As an earlier chapter focused exclusively on low-income owners (those with household incomes below $50,000) this chapter will place particular emphasis on owner households with incomes greater than $50,000.

POPULATION GROWTH

Prior to the recession, the City of Madison saw modest population growth in line with historic averages driven primarily by owner households and relatively large household sizes (more than two people) while the rental market was stagnant. **After the recession, Madison's population growth shifted into a higher gear, resulting in a measurably higher household growth rate, however owner households barely increased.**

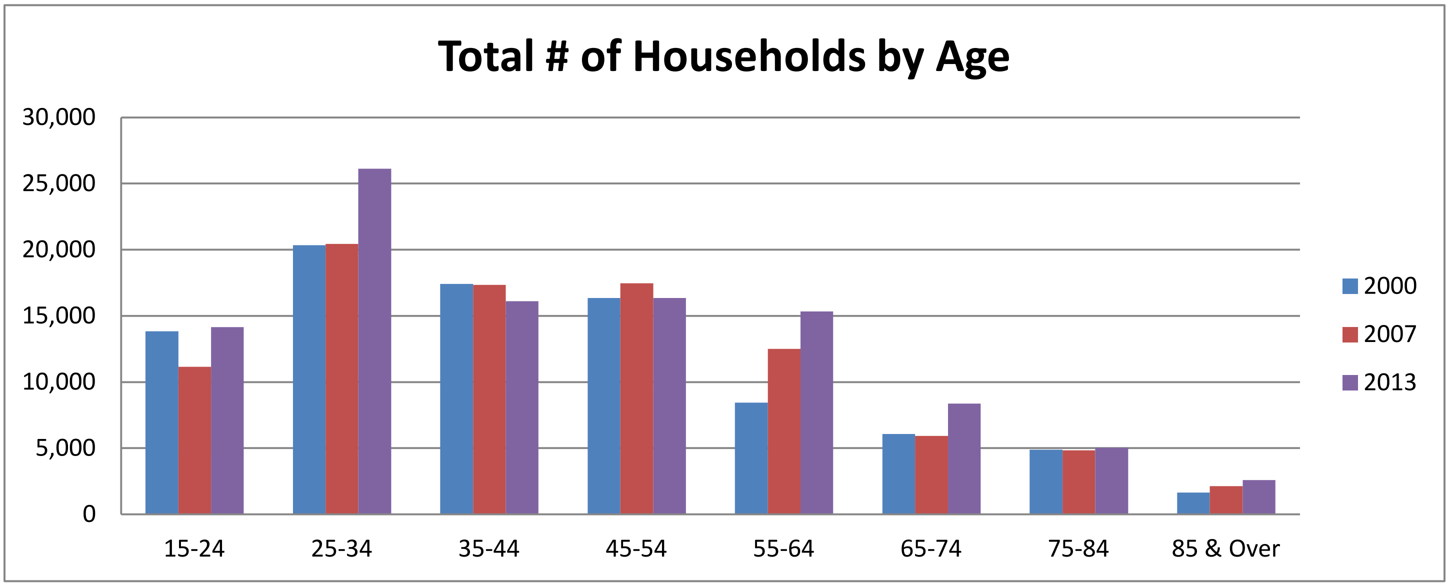
	2000 Census to 2005-2007 ACS		2005-2007 ACS to 2011-2013 ACS	
	Annual Growth Rate	Total Growth	Annual Growth Rate	Total Growth
Population	1%	6%	1.5%	9%
Households	0.5%	3%	2%	13%
Renter Households	-1%	-7%	4%	25%
Owner Households	2%	14.5%	0.5%	3%



Source: 3-year American Community Survey

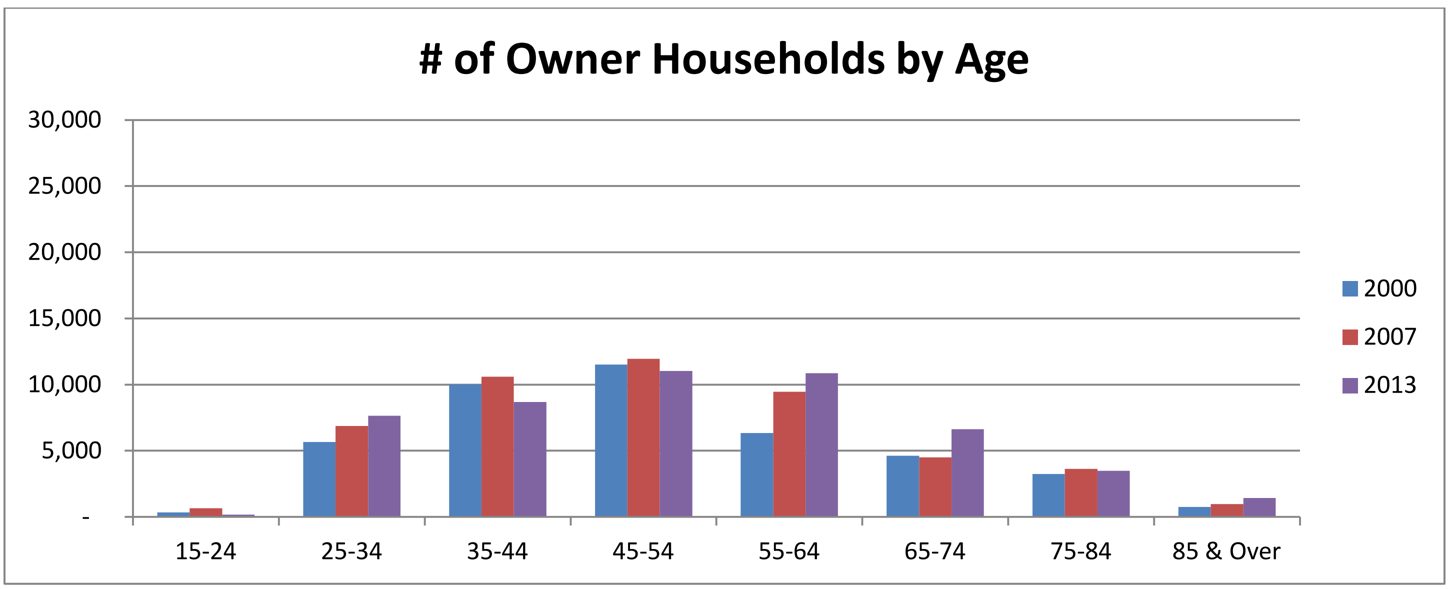
The combination of strong household growth and clear preference for rental housing made **Madison a majority renter community in 2011**.

HOUSING TENURE BY AGE

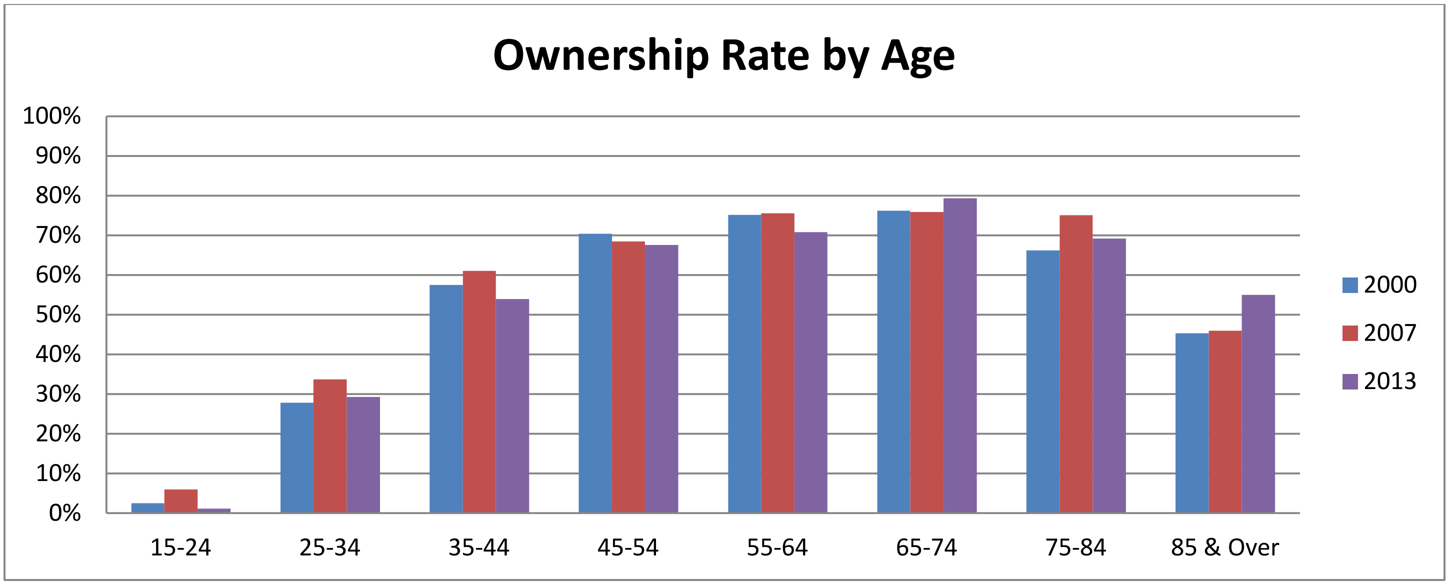


Source: 2000 Decennial Census, 3-year American Community Survey

While our overall population mix has shifted to be younger due to the large influx of Millennials (25-35 year olds), our homeownership mix has shifted to be older. **Over the last 15 years, our home owning population has noticeably shifted so that roughly half of homeowners are 55 or older**.

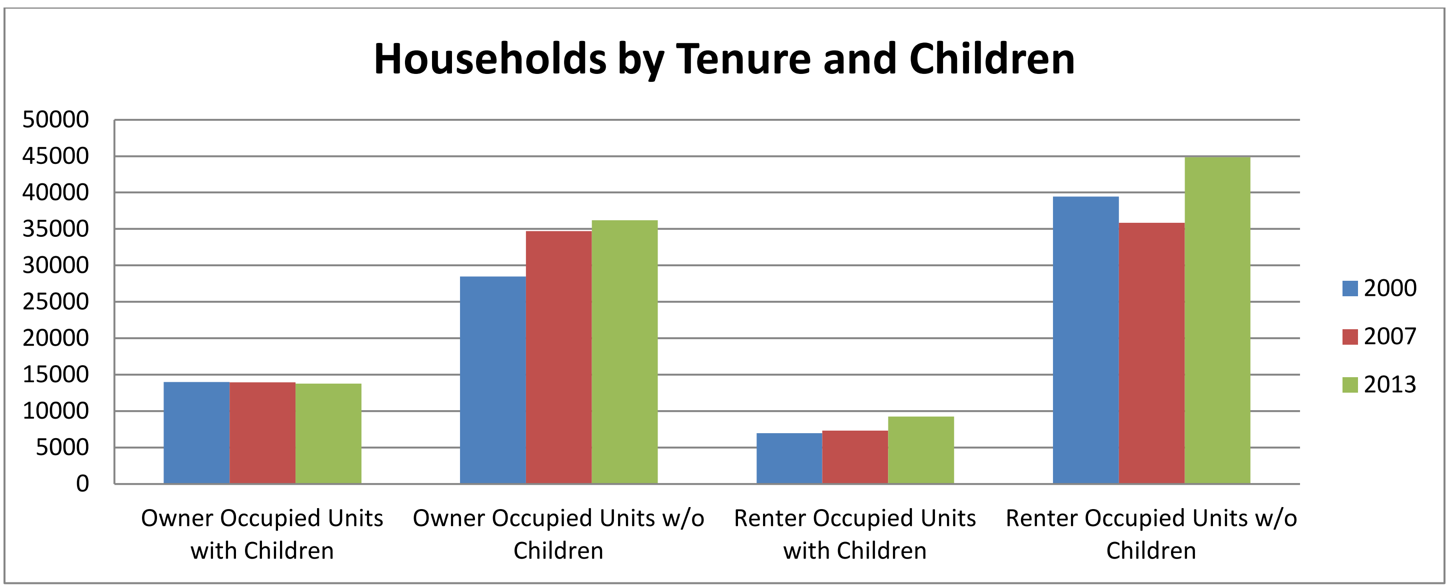


Source: 2000 Decennial Census, 3-year American Community Survey



Source: 2000 Decennial Census, 3-year American Community Survey

The second major trend in ownership is that all growth is coming from households without children. The number of owner occupied housing with children has been flat for 15 years.

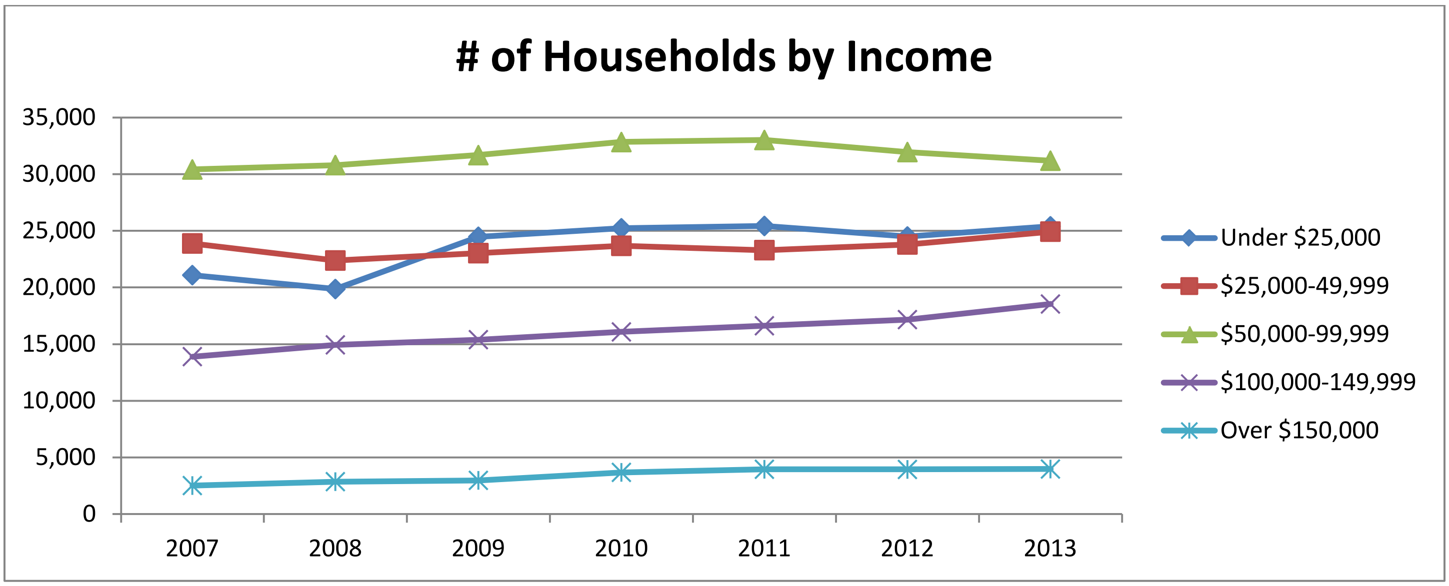


Source: 2000 Decennial Census, 3-year American Community Survey

HOUSING TENURE BY INCOME

Traditionally, Madison has seen a strong correlation between income and ownership rates. This implies that growth in low-income households would increase demand for rental housing while growth in high-income households would increase demand for owner housing. **After the recession, growth has been split between very low-income households and relatively affluent households, with little net growth in the middle.** Since 2007, the City of Madison has added approximately:

- 12,200 new households
- 4,300 households with incomes below $25,000 (<40% of Median Household Income)
- 1,000 households with incomes $25,000 to $49,999 (40-80% of Median Household Income)
- 800 households with incomes $50,000 to $99,999 (80-160% of Median Household Income)
- 2,700 households with incomes $100,000 to $149,999 (160-240% of Median Household Income)
- 3,400 households with incomes $150,000 and above (>240% of Median Household Income)



Source: 3-Year American Community Survey

Household Growth Rate 2007-2013

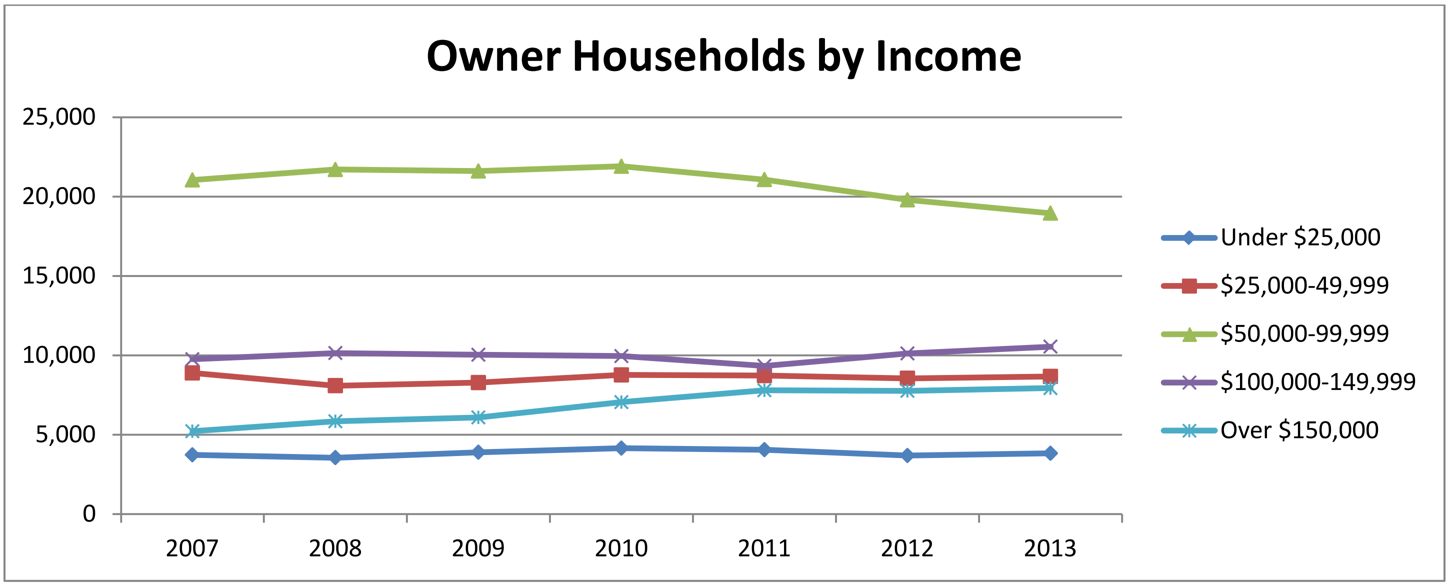
	Average Annual Growth Rate	Total Growth
Total	2%	13%
Under $25,000	3%	20%
$25,000-49,999	1%	4%
$50,000-99,999	0.4%	3%
$100,000-149,999	4%	24%
Over $150,000	8%	61%

The ownership market has been relatively stagnant at all but the highest income levels. The ownership market has only absorbed 10% of households added to the City since 2007.

Since 2007, the City of Madison has added approximately:

- 1,300 new owner households
- 100 owner households with incomes below $25,000 (<40% of Median Household Income)
- -200 owner households with incomes $25,000 to $49,999 (40-80% of Median Household Income)
- -2,100 owner households with incomes $50,000 to $99,999 (80-160% of Median Household Income)
- 800 owner households with incomes $100,000 to $149,999 (160-240% of Median Household Income)
- 2,700 owner households with incomes $150,000 and above (>240% of Median Household Income)

Compared to the rental market, the homeownership market has grown relatively slowly**. Moreover, middle class ownership households with incomes of $50,000-$99,999 saw a 10% decline over this period. Virtually all growth in homeownership has come from higher income households.**



Source: 3-year American Community Survey

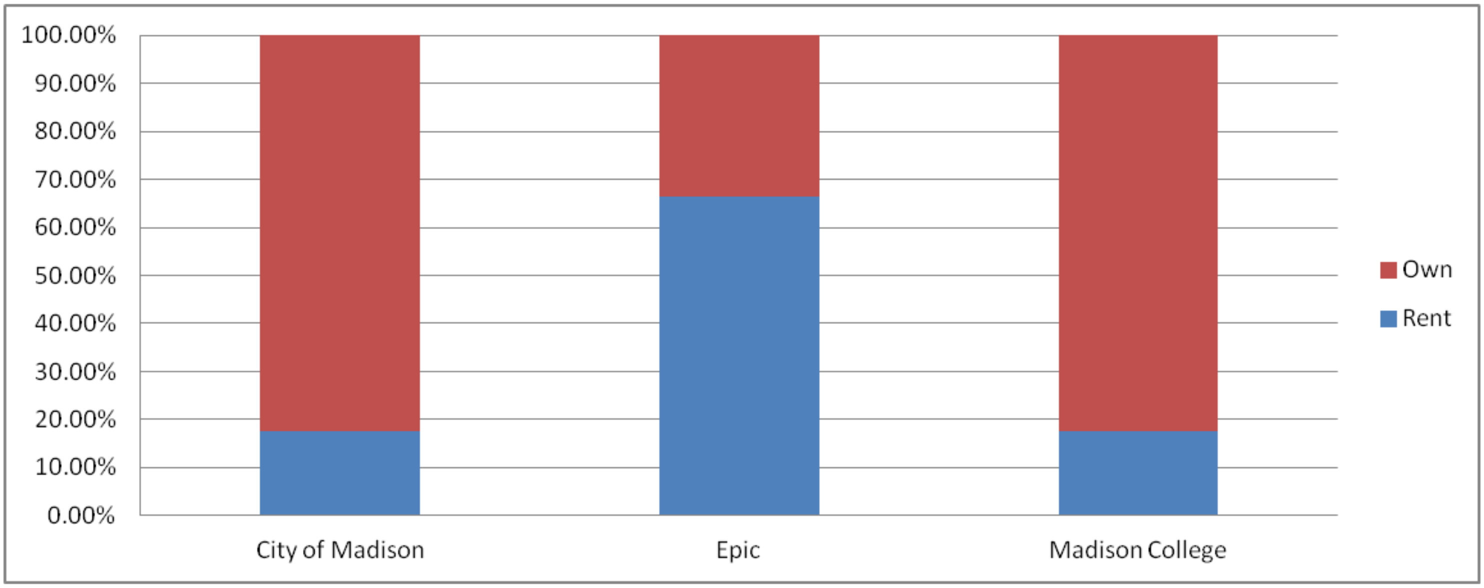
Homeownership Growth Rate 2007-2013

	Average Annual Growth Rate	Total Growth
Total	0%	3%
Under $25,000	0%	3%
$25,000-49,999	0%	-2%
$50,000-99,999	-2%	-10%
$100,000-149,999	1%	8%
Over $150,000	7%	52%

HOUSING PREFERENCES

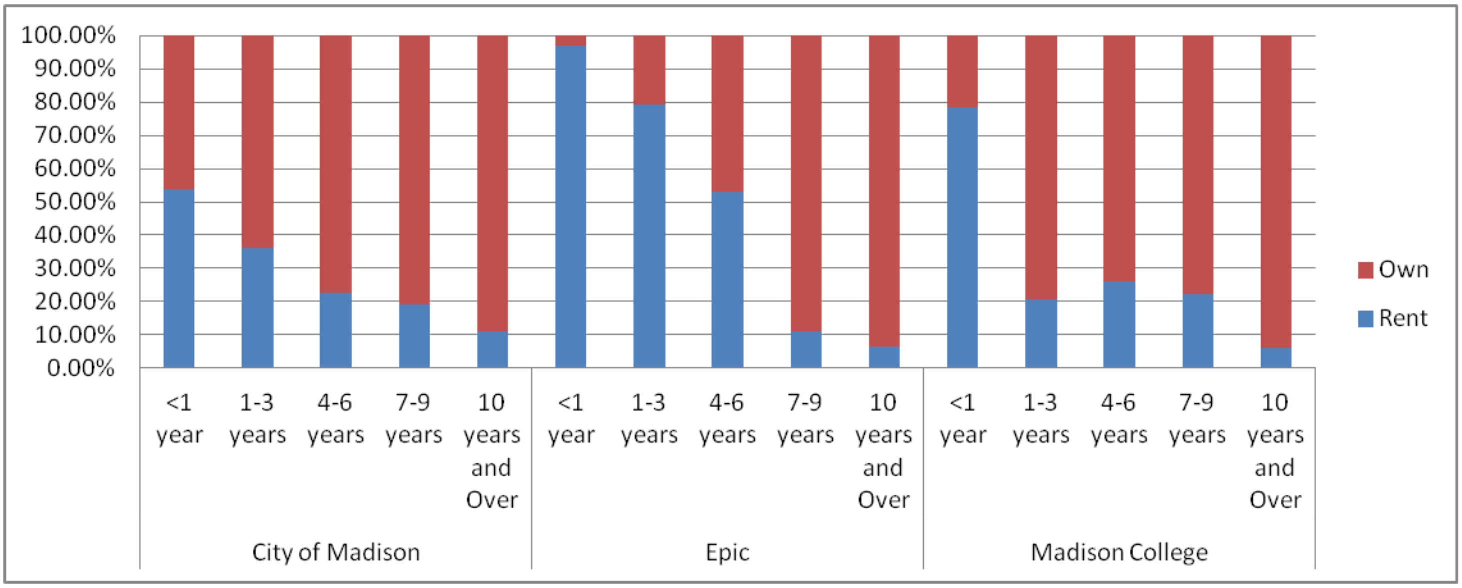
Combining all of the trends in the data, it is clear that there has been a shift in housing preferences towards rental and that there are new hurdles to homeownership holding back those who do want to own. To better understand this demand, the City of Madison commissioned a survey on housing preferences from area employers including the City of Madison, Epic, and Madison College (Appendix A). These employers serve as a reasonable proxy for three of the primary employment sectors in Madison (government, technology, and higher education). From these data, a number of trends appear.

RENT VS OWN



Source: 2014 City of Madison Housing Survey

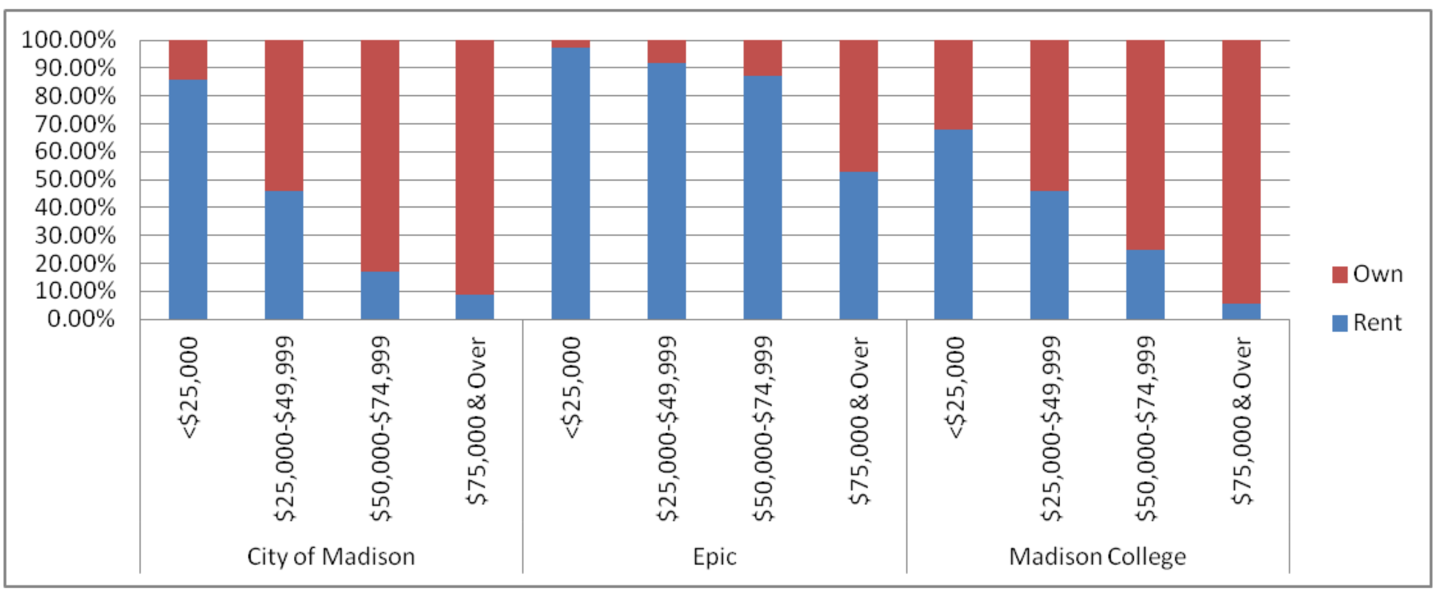
RENT VS OWN BY LENGTH OF EMPLOYMENT



Source: 2014 City of Madison Housing Survey

First, there is a very close correlation between the length of time an employee has worked for their current employer and their rate of homeownership. This relationship holds across all employers. This relationship indicates that **the longer an employee stays with their employer (and presumably in the community) the more likely they are to purchase a home.**

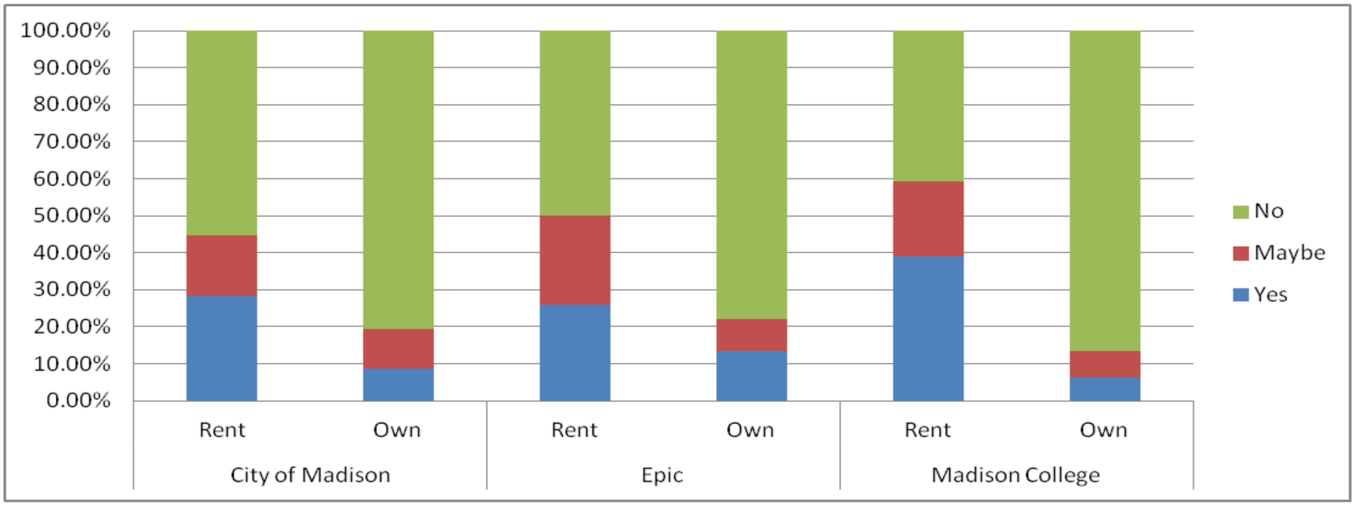
RENT VS OWN BY HOUSEHEOLD INCOME



Source: 2014 City of Madison Housing Survey

Second, just as in the Census data a clear correlation exists between higher incomes and higher rates of homeownership regardless of employer**.** However, **the data indicate that the length of time an employee has worked for their employer can trump income, as we see a significant number of higher income employees that are relatively new to their positions choosing to rent**.

INTEREST IN PURCHASING IN THE NEXT 2 YEARS



Source: 2014 City of Madison Housing Survey

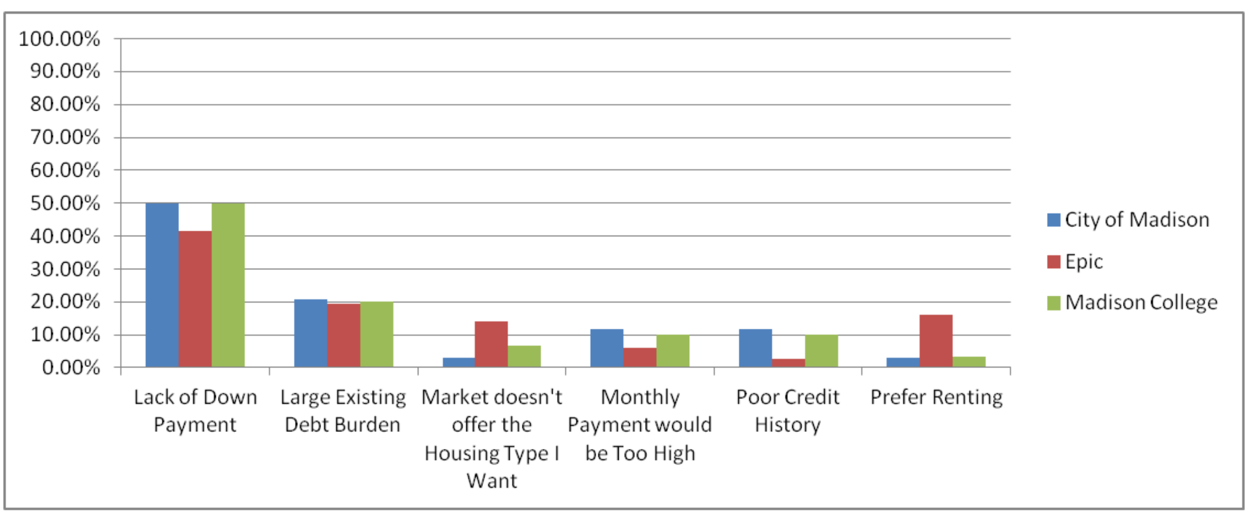
Renters, when asked if they planned to purchase a home in the next two years, 50% said no, 25% said maybe and 25% said yes. For those in the yes and maybe categories, a few factors prohibiting ownership dominated:

- The primary financial barrier was a lack of down payment with existing debt (presumably student debt) in second
- The actual monthly cost of ownership was seen as a very small barrier
- The largest non-financial barriers were "Prefer to Rent" and "Other" which largely consisted of comments regarding timing and uncertainty about commitment

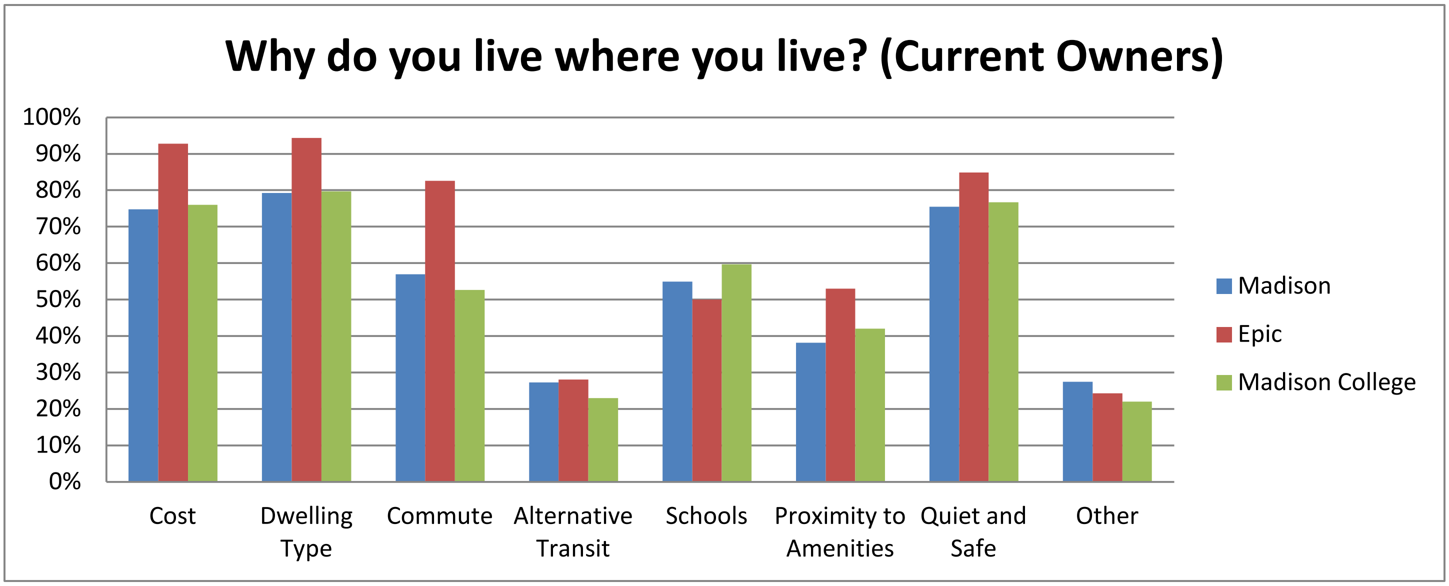
These data support the argument that it is not simply cost that is preventing renters from purchasing. Instead, there are number of factors that lead to renters not being ready at this point in their lives and careers to make a financial and personal commitment to ownership.

Furthermore, comments regarding "Market doesn't offer the Housing Type I Want" focused on the lack of condominium and townhouse products in central locations (29% of likely buyers stated these as their preferred housing types)

MAIN BARRIER TO PURCHASING



FACTORS IN CURRENT HOUSING SELECTION – CURRENT OWNERS



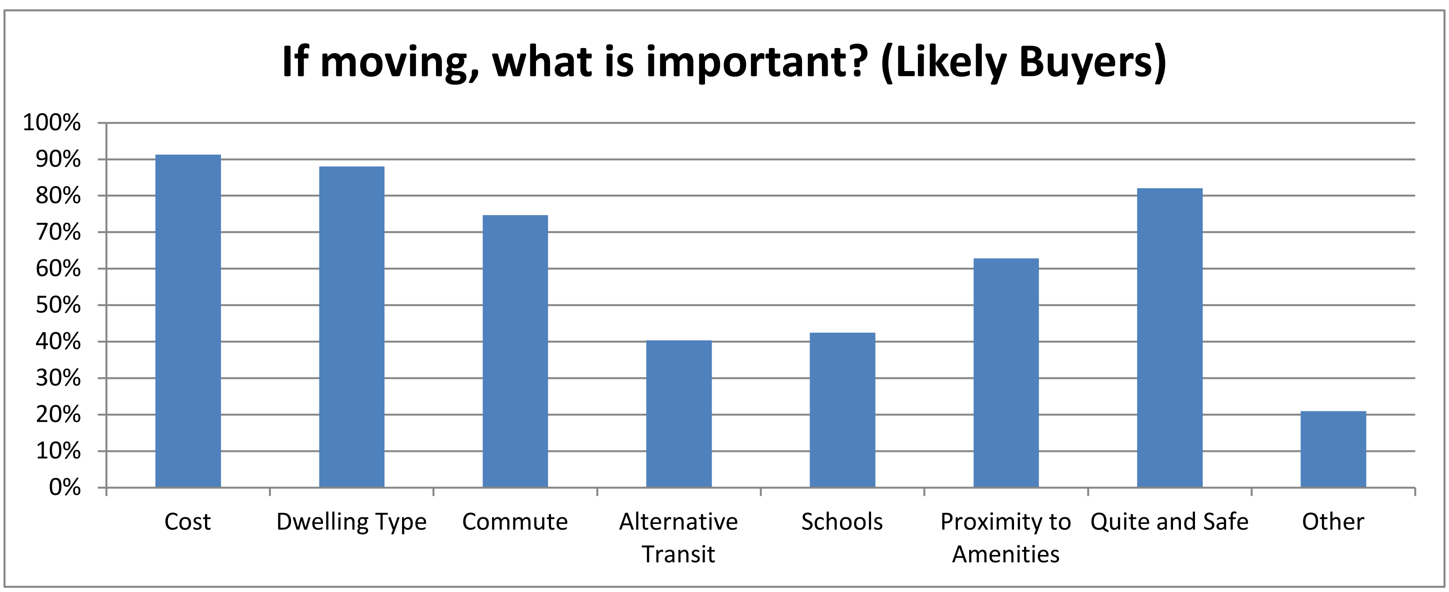
Source: 2014 City of Madison Housing Survey

When asked why current owners live where they do a few clear trends emerged:

- The unit itself is universally important as shown by responses regarding the cost and type of unit
- Location is somewhat less important, as shown by lower responses for Commute, Alternative Transit, and Proximity to Amenities (but not quiet and safe neighborhood)

When asked what factors matter to renters and owners planning to purchase in the next two years, a slightly different pattern emerges as locational factors of Commute, Alternative Transit, and Proximity to Amenities are greater priorities to those planning to purchase than they are to our current homeowners. **These results support recent studies confirming that 25-34 year olds have experienced a strong preference shift placing a premium on proximity to amenities when choosing housing**.

FACTORS IN CURRENT HOUSING SELECTION - LIKELY BUYERS

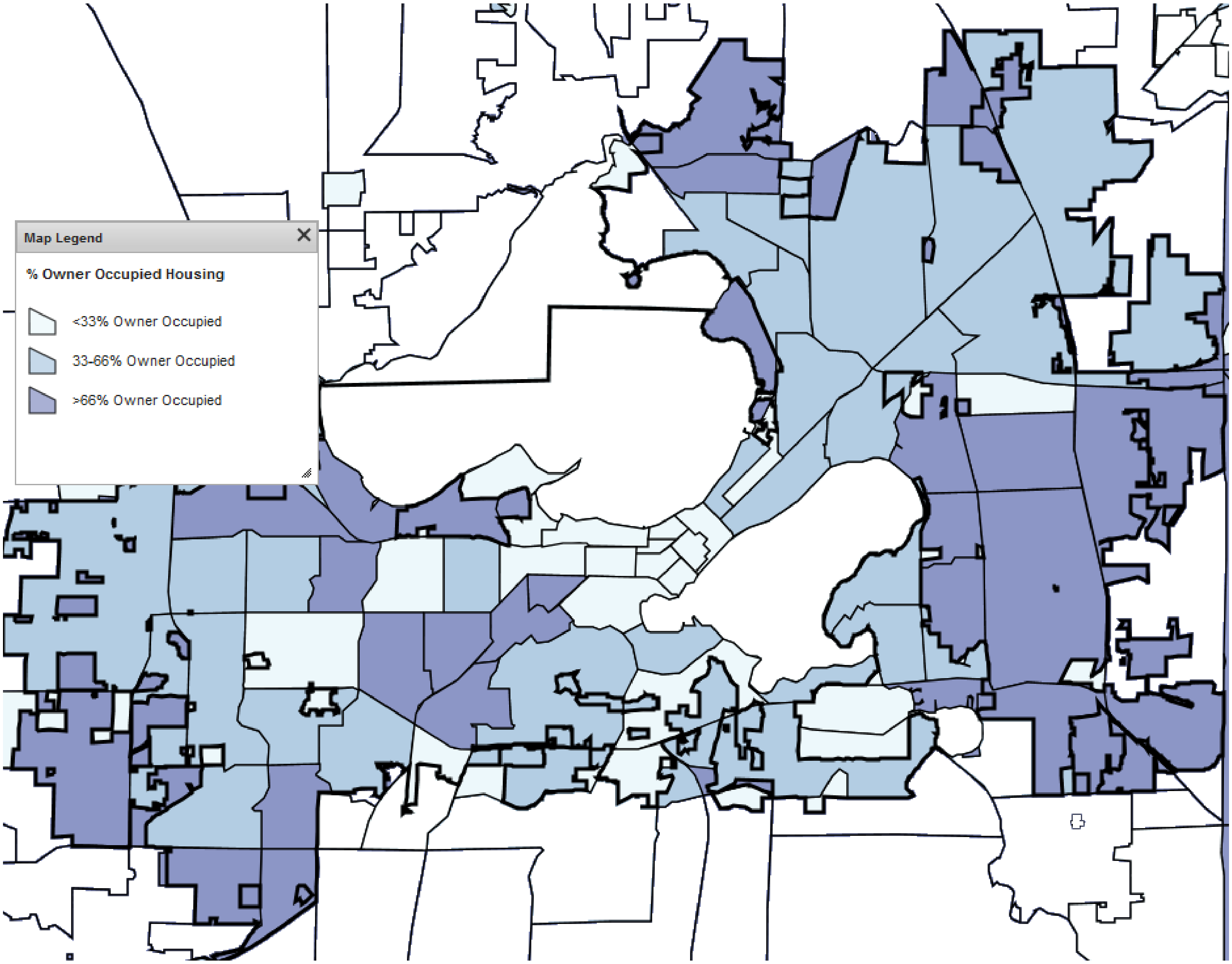


Segregating households with children from those without, a noticeably different set of priorities emerges as quality of schools becomes a significant factor in selecting where to live. Of households planning to purchase in the next two years that have children in the household, 90% consider the quality of schools an important factor in choosing where to live compared to only 27% of households without children.

TRENDS

- Compared to 2000 and 2007, today's homeowner is:
    - Older
    - Wealthier
    - Less likely to have children in the home
- Middle class households are leaving or failing to enter the ownership market
    - Significant loss of $50,000-$100,000 (80%-160% of AMI) households
    - Only 30% of new households at $100,000-$150,000 (160%-240% of AMI) were/became homeowners
        - Despite likely having the financial means to purchase
- New households are not entering the ownership market
    - 9 out of 10 households added since 2007 chose to rent
    - Homeownership rates in younger age groups have dropped since 2010
- Preferences are shifting
    - The next generation of likely buyers puts a premium on the location of their housing (Commute, Alternative Transit, and Proximity to Amenities) compared to previous generations of buyers
    - The majority of potential buyers do not have children (yet) or place much emphasis on schools when choosing housing locations
        - But those with children place extra emphasis on schools

HOUSING STOCK



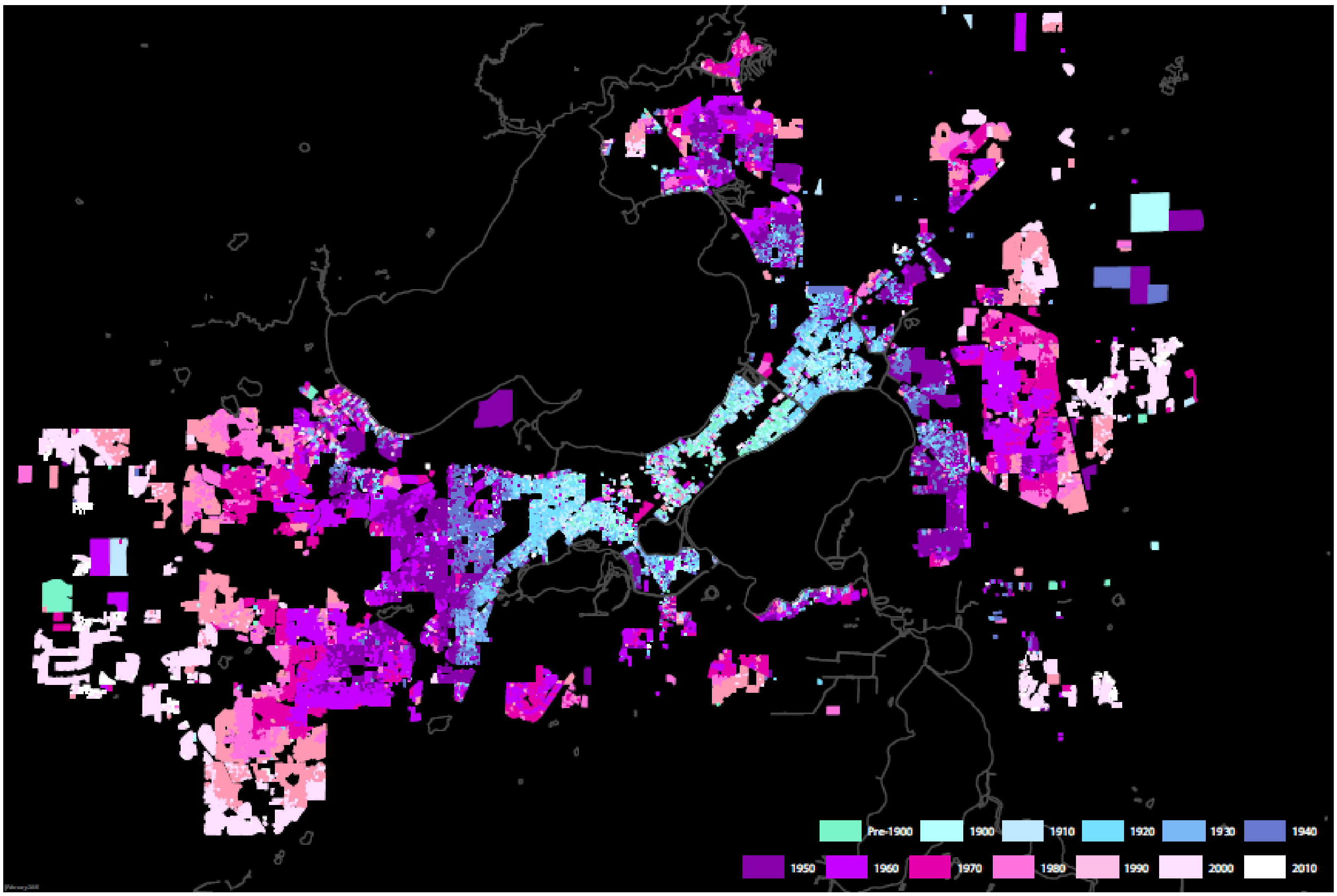
Source: HUD CPD Maps

In the City of Madison, the stock of owner occupied housing is not equally distributed across the city. Centrally located neighborhoods and commercial/transportation corridors have a mix of owner and rental housing. Broad swaths of the west and east sides as well as the city edge have significantly higher concentrations of owner occupied housing stock.

This pattern is partially the result of market forces and city planning that has denser multifamily development in centrally located neighborhood and commercial/transportation corridors. It is also a product of when areas of the city developed. The most centrally located neighborhoods were originally developed over 100 years ago and as the housing became obsolete it was largely converted to or replaced with commercial buildings and rental housing.

Madison saw significant population growth and development in the decades following World War II resulting in the creation of subdivisions dominated by single family owner occupied housing on the north, east, west, and southwest sides.

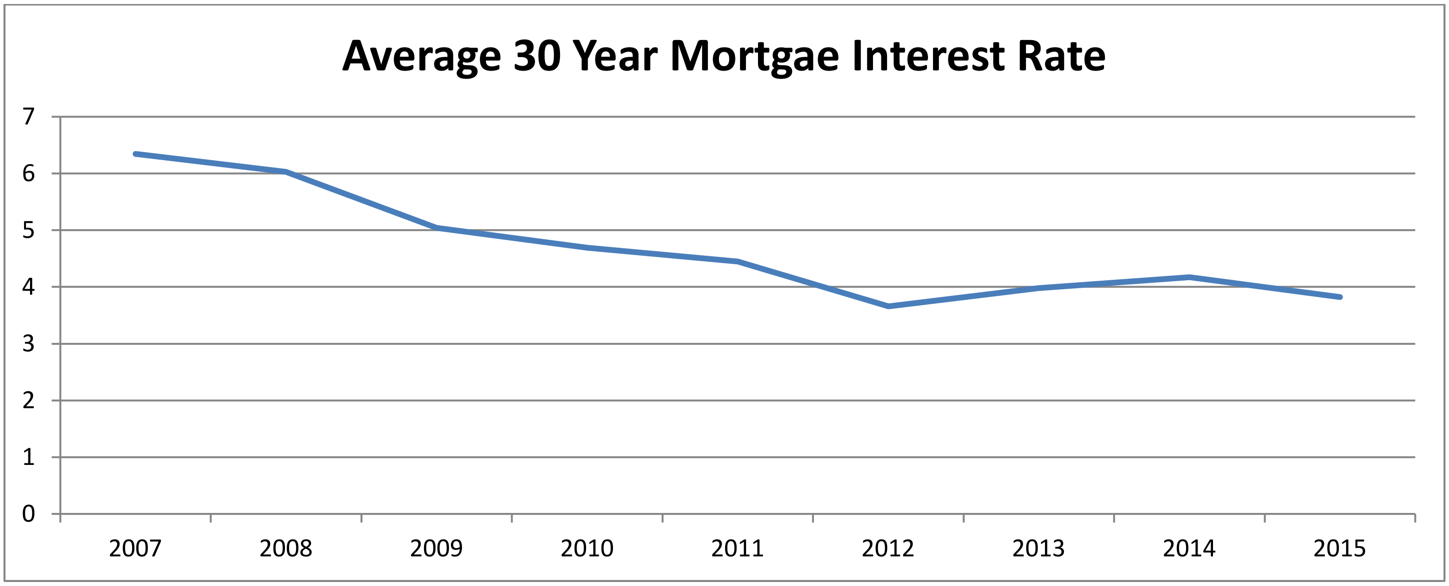
More recent subdivisions have been created along the edges of the city, but in general they have been smaller in scale than post World War II subdivisions and many have a rental or commercial component breaking up the concentration of single-family owner occupied homes.



HOUSING COST, PRICE, AND VALUES

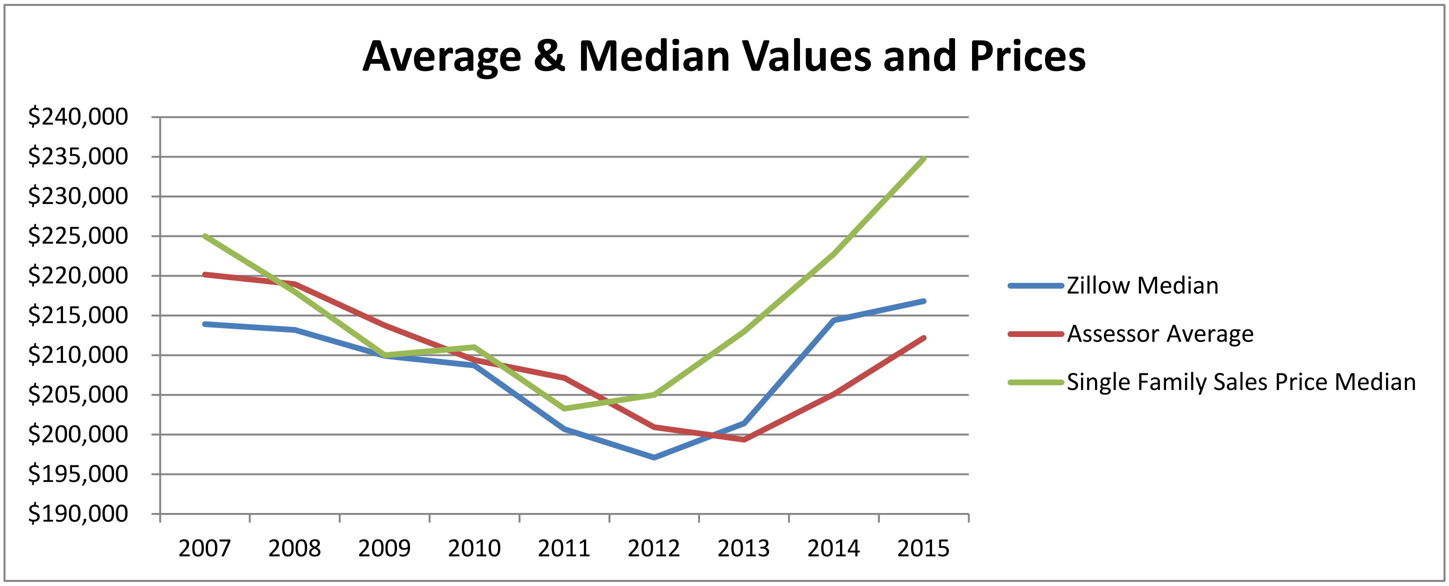
The cost of ownership is driven by three primary factors: housing prices, interest rates, and property tax rates**. Due to the decline in prices and historically low interest rates, home ownership is more affordable than ever**.

Housing prices and interest rates in general are negatively correlated because lower interest rates increase the amount that a buyer can afford to borrow, therefore raising prices. Theoretically property tax rates are somewhat correlated to interest rates because high interest rates raise government expenses and property tax rates are negatively correlated to housing prices because high property values increases the property tax base, which allows for lower property tax rates. Other housing costs include property insurance, utilities, fuel, water, garbage collection, and homeowner association fees, which all add up to thousands of dollars per year for a typical home (these costs are included in American Community Survey cost measures)



Interest rates continue to hold at or near historic lows, making homeownership more affordable.

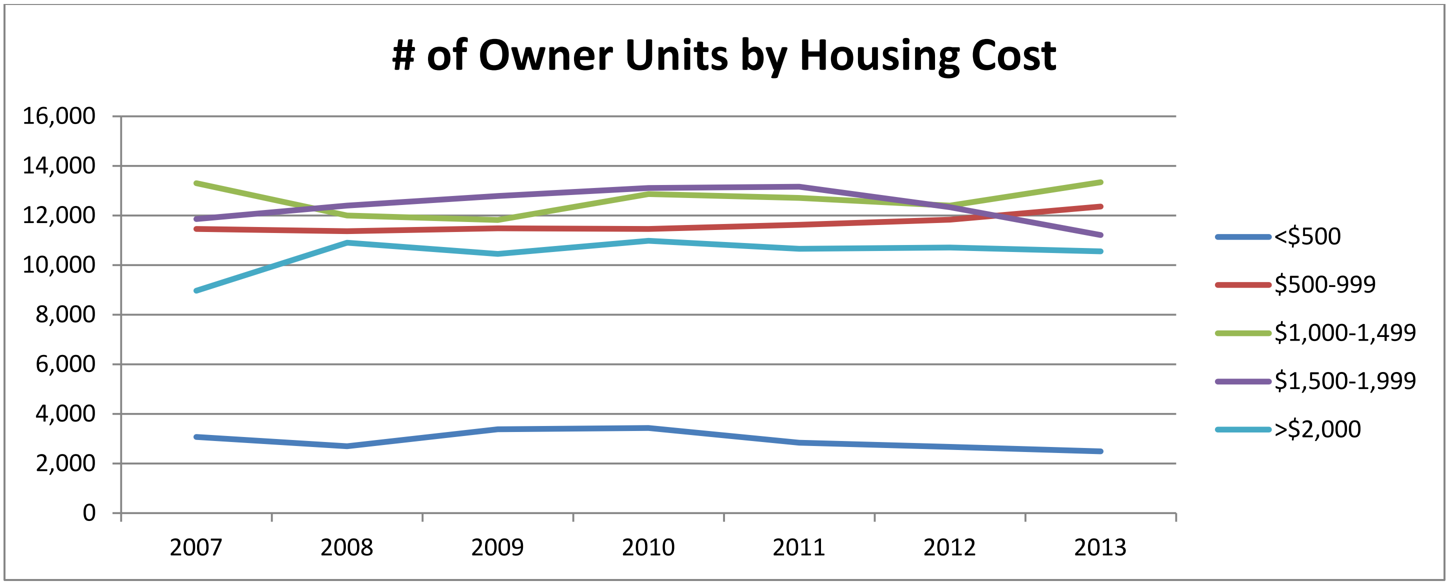
The 2007 recession was in part caused by the bursting of a credit driven housing bubble. The result was a nationwide drop in house values. In response, the Federal Reserve dropped interest rates effectively to zero to stimulate a recovery. **The combination of reduced home prices and historically low interest rates reduced the theoretical cost of ownership** dramatically in Madison. This effect was somewhat mitigated by property tax rates which continued to rise during this period.



The median prices (50th percentile as computed by Zillow, a data aggregator) and average home values (total assessed value divided by number of units as computed by the Assessor's Office) as well as sale price in the City of Madison for single family homes dropped significantly after the start of the recession and only recently began to rise again, which should have made homeownership more affordable. For example, the average house in 2007 was assessed at $220,150. Assuming a 20% down payment and average mortgage interest rate of 6.25%, monthly mortgage payments would be $1,085 with a tax payment of $365 totaling $1,450 per month. **In 2012, the average house assessment had dropped to $201,000 and interest rates had gone down to 4% resulting in monthly payments of $770 and taxes increased to $400, resulting in a 19% reduction in average housing cost.** Today, average assessments have returned to pre-recession values, but interest rates remain at a near record low of 4%, resulting in a typical monthly mortgage and tax payment of $1,235.

	Average Home Value	Interest Rate	Monthly Mortgage Payment	Monthly Property Tax	Total Monthly Payment
2007	$220,150	6.25%	$1085	$365	$1,450
2012	$201,000	4.00%	$770	$400	$1,170
2015	$212,175	4.00%	$810	$425	$1,235

Assuming $50 per month insurance costs, in 2007 the typical home required an annual income of $60,000 (~100% of Area Median Household Income) while **in 2015, the typical home only required an annual income of $51,000 (80% of Area Median Household Income)**. (*Assumes a 20% downpayment, low amounts of non-housing debt, and 30% of income spent on housing costs)



Unit Growth Rate 2007-2013

	Average Annual Growth Rate	Total
Less than $500	-4%	-22%
$500-$999	2%	12%
$1,000-$1,499	8%	65%
Over $1,500	12%	108%

Source: 3-Year American Community Survey

However, **according to Census data households did not realize a net reduction in housing costs**. Instead, the Census reported rising housing costs for homeowners. This could be because homeowners stayed in their existing home negating the drop in home value, rising property taxes, or an increase from property insurance, utilities, fuel, water, garbage collection, homeowner association fees, or mobile home fees that are also included in Census statistics. Another likely culprit is the inability of many homeowners to refinance their mortgage to the new lower rates due to their reduced home equity.

While citywide median values give a picture of the overall market, households looking to purchase segment the market by geography and by price. To illustrate patterns in price and geography, the market can be segmented into:

Starter Homes

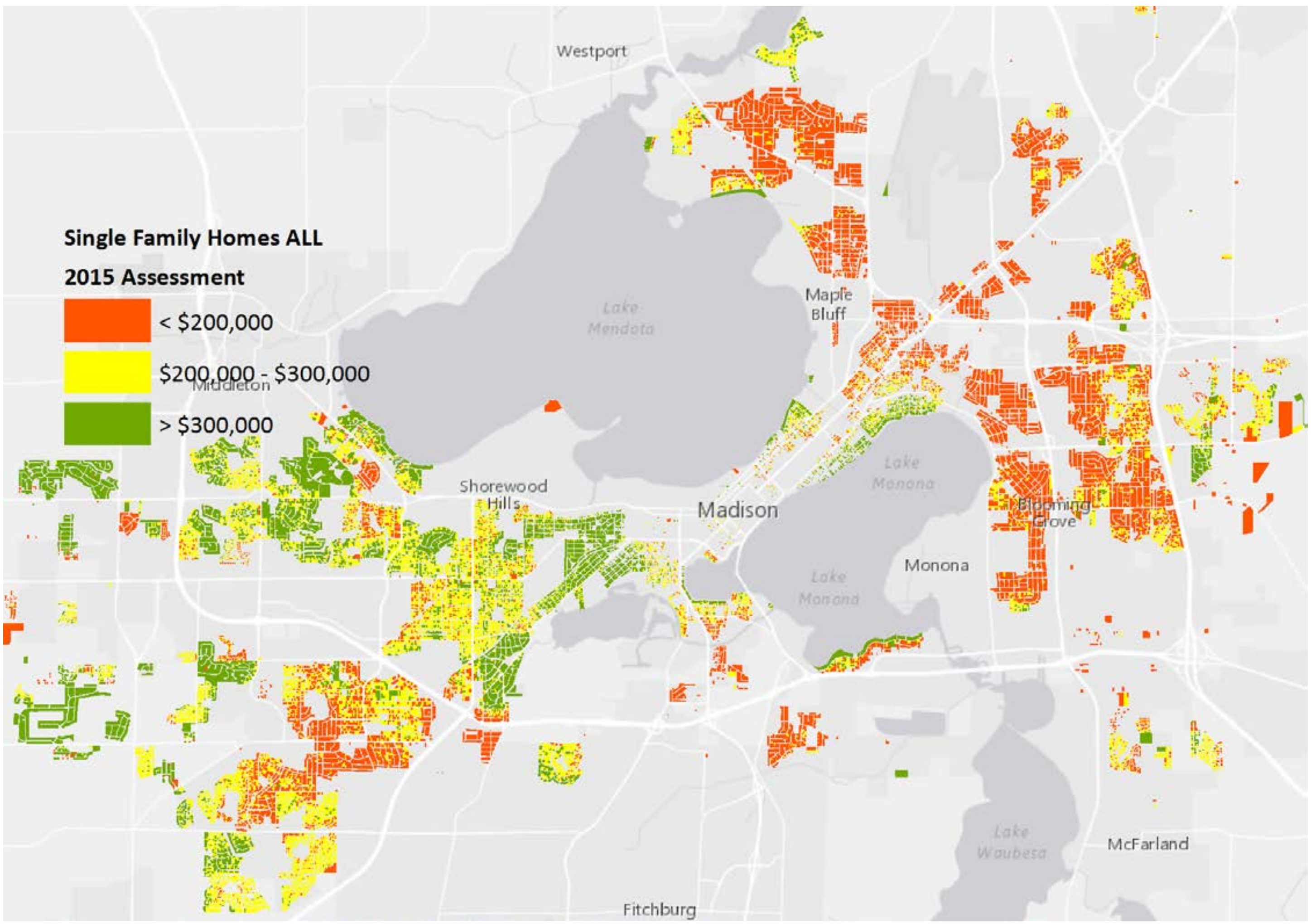
- The least expensive 1/3 by list price
- Under $200,000 in the City of Madison

Mainstream Homes

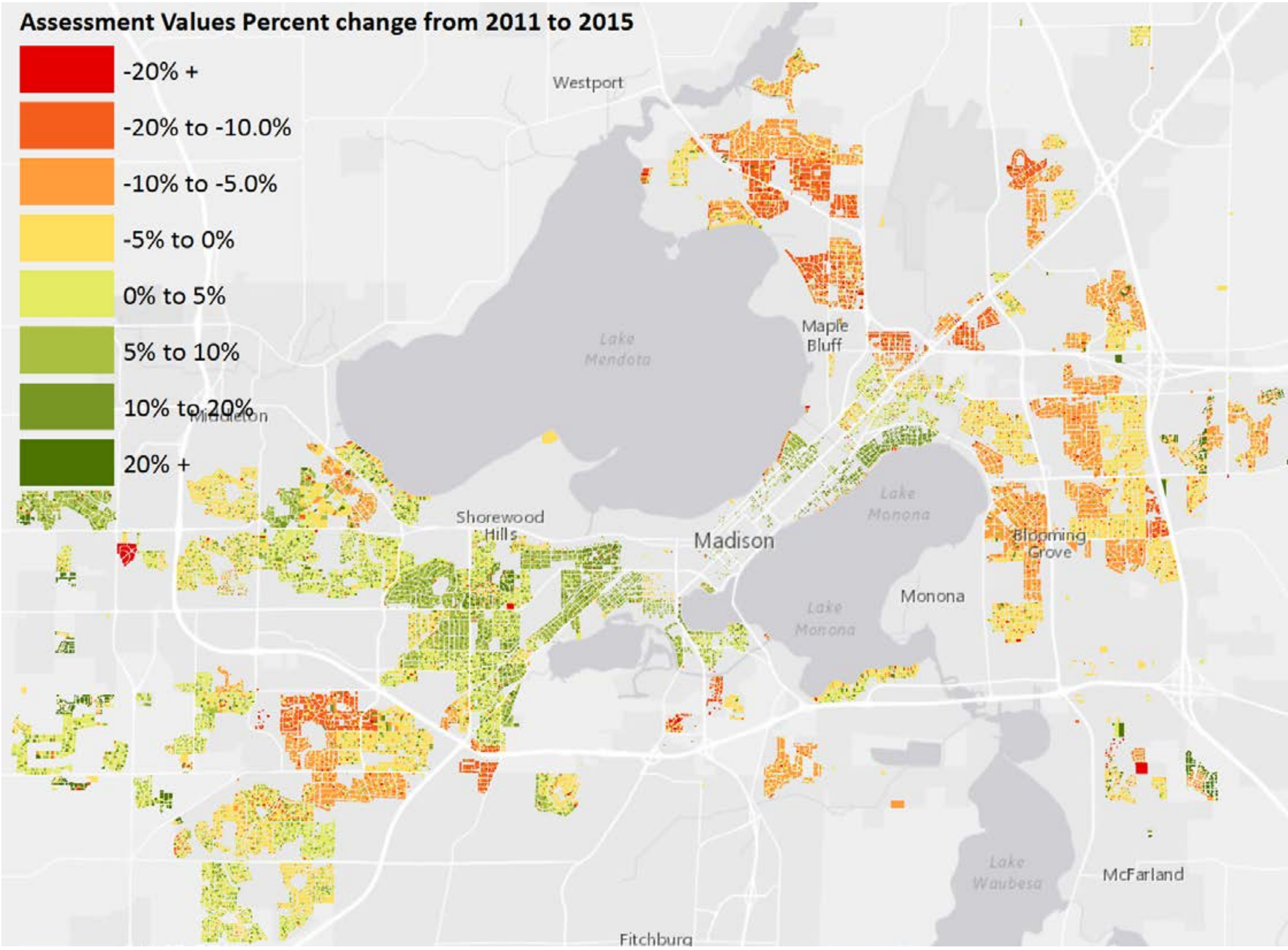
- The middle 1/3 by list price
- $200,000 to $300,000 in the City of Madison

Premium Homes

- The most expensive 1/3 by list price
- Over $300,000 in the City of Madison



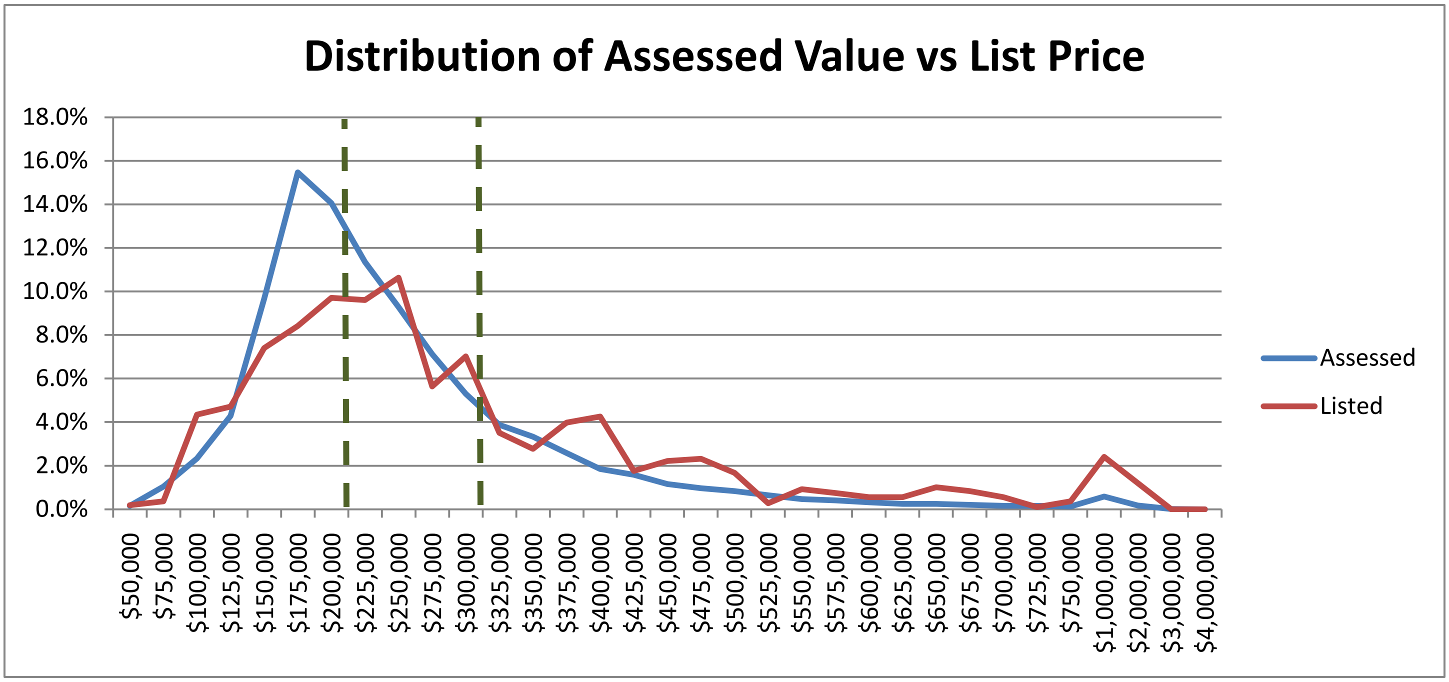
The general pattern is higher values in neighborhoods that are closer to downtown and have older homes (pre-WWII) as well as in neighborhoods on the city edge that have relatively new houses (post-1990). Neighborhoods dominated by mid-century housing stock are more mixed in value, which is likely driven by lot size, house size, and neighborhood amenities.



The geographic pattern of changes in assessed value from 2011 to 2015 shows a very uneven recovery with centrally located near east and near west neighborhoods as well as far west and southwest side neighborhoods recovering value and seeing greater appreciation than the north, east, and southwest sides. This pattern demonstrates a strong market desire for the location, type, age, or prices in those neighborhoods.

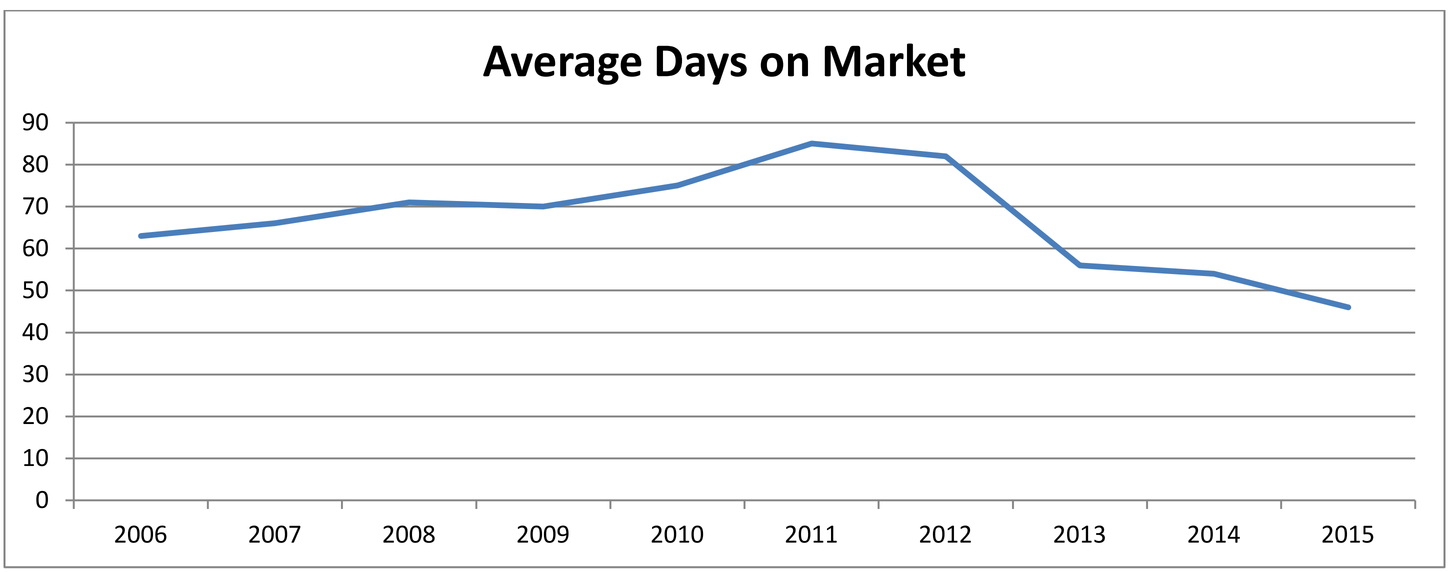
HOME INVENTORY

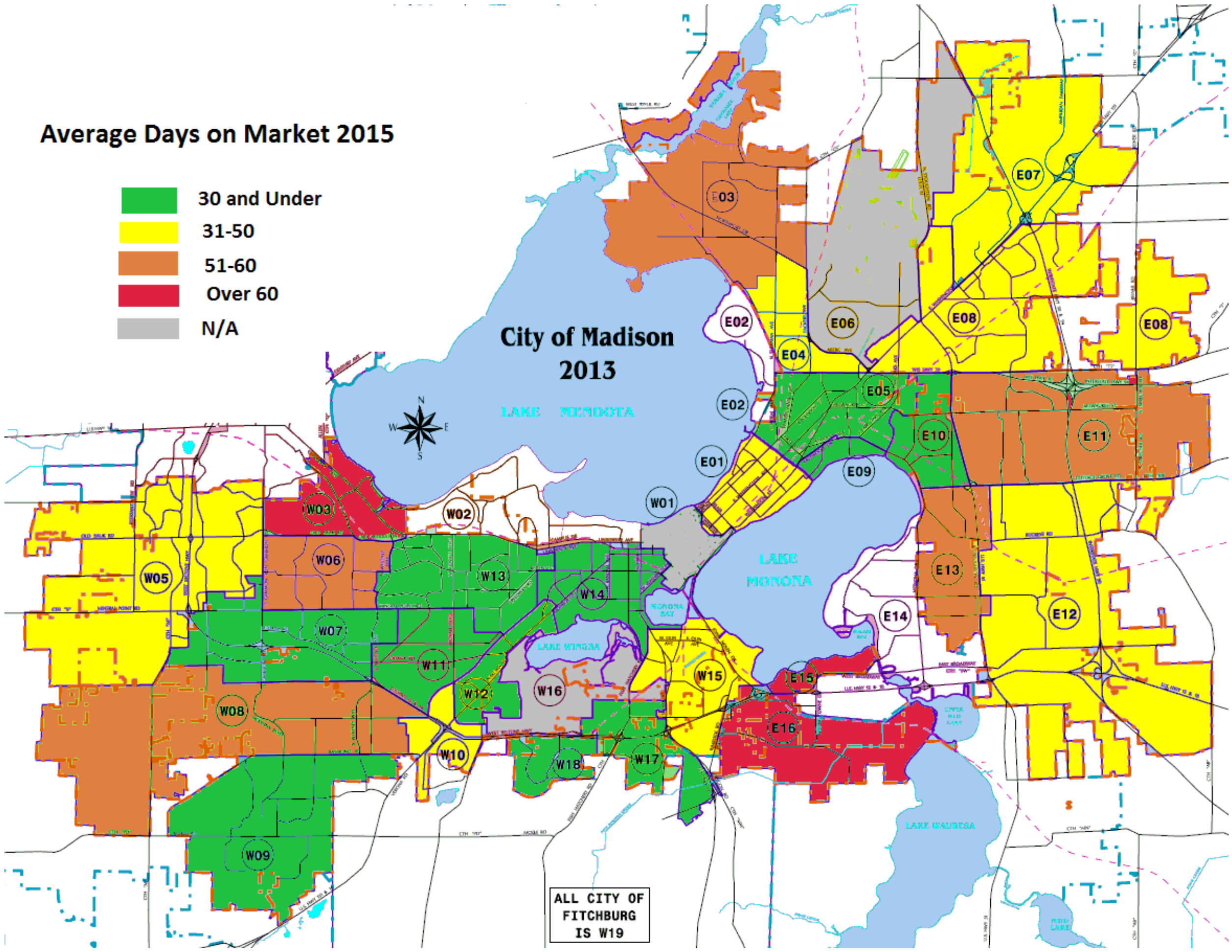
Nationally, regionally, and locally the inventory of homes for sale has dropped dramatically since the housing market recovery began. This low inventory has lead to a very competitive market for homes in Madison. It is common for homes to have multiple offers and sell within a few days of being listed for sale. However, this inventory tightness is not universal across all price points.



Generally, inventory has dropped for Starter and Mainstream homes, but less so for Premium homes. Comparing the distribution of assessed values of Madison's existing stock to what is currently listed for sale, it appears that the market has shifted upwards in price. This is likely caused by a combination of general price increase due to a recovering economy (assessments have not caught up yet) and greater inventory tightness for Starter and Mainstream homes.

Since peaking in 2011-2012, the average amount of time that a single family home stays on the market has dropped dramatically to an average of 44 days in 2015. This is not uniform across the City, with neighborhoods on the near east, near west, and far southwest sides staying on the market for significantly less time.





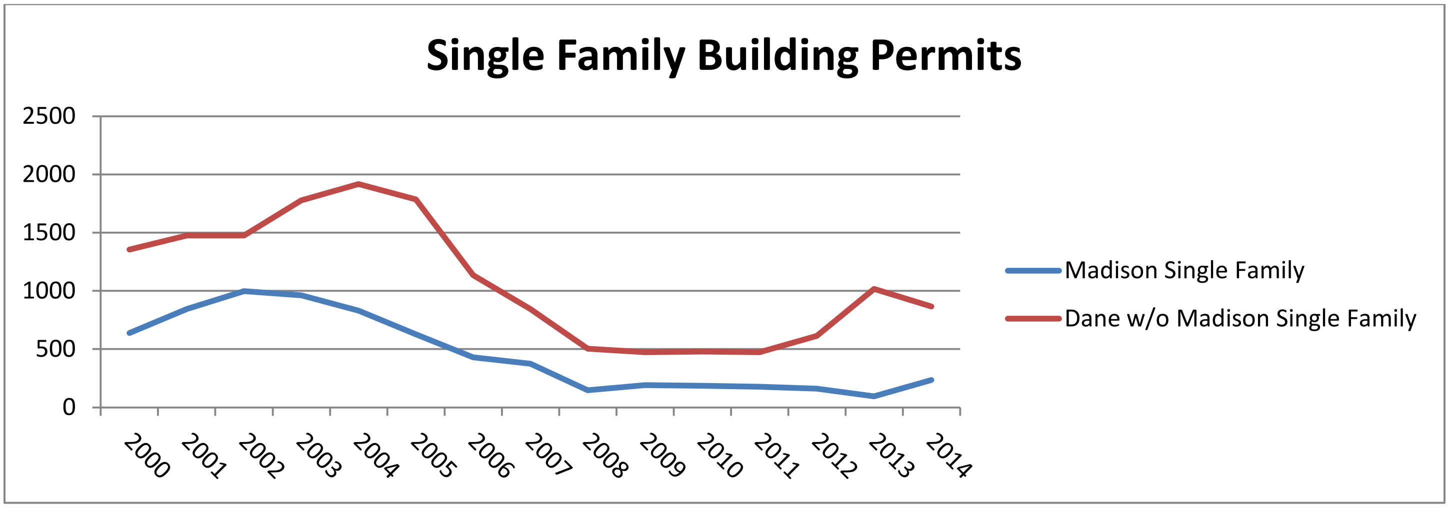
*Areas W17 and W18 only saw a handful of transactions which may not be representative of the larger neighborhood market

When combined with the change in assessment data, the pattern of days on market hint at neighborhoods where the single family housing stock is not matching the demands of the market. These neighborhood can be considered an “Opportunity” in that they currently represent a bargain in our housing market. These neighborhoods contain an abundance of housing that is currently priced as “Starter Homes” that could be nudged into “Mainstream” with strategic investment. In general these neighborhoods have:

- Moderate to high percentage of owner occupied homes
- 40+ year old housing stock
- Average property value below the City average
- Longer than average days on market
- Flat or declining assessed values
- Located between more centrally located urban/walkable neighborhoods and newer development

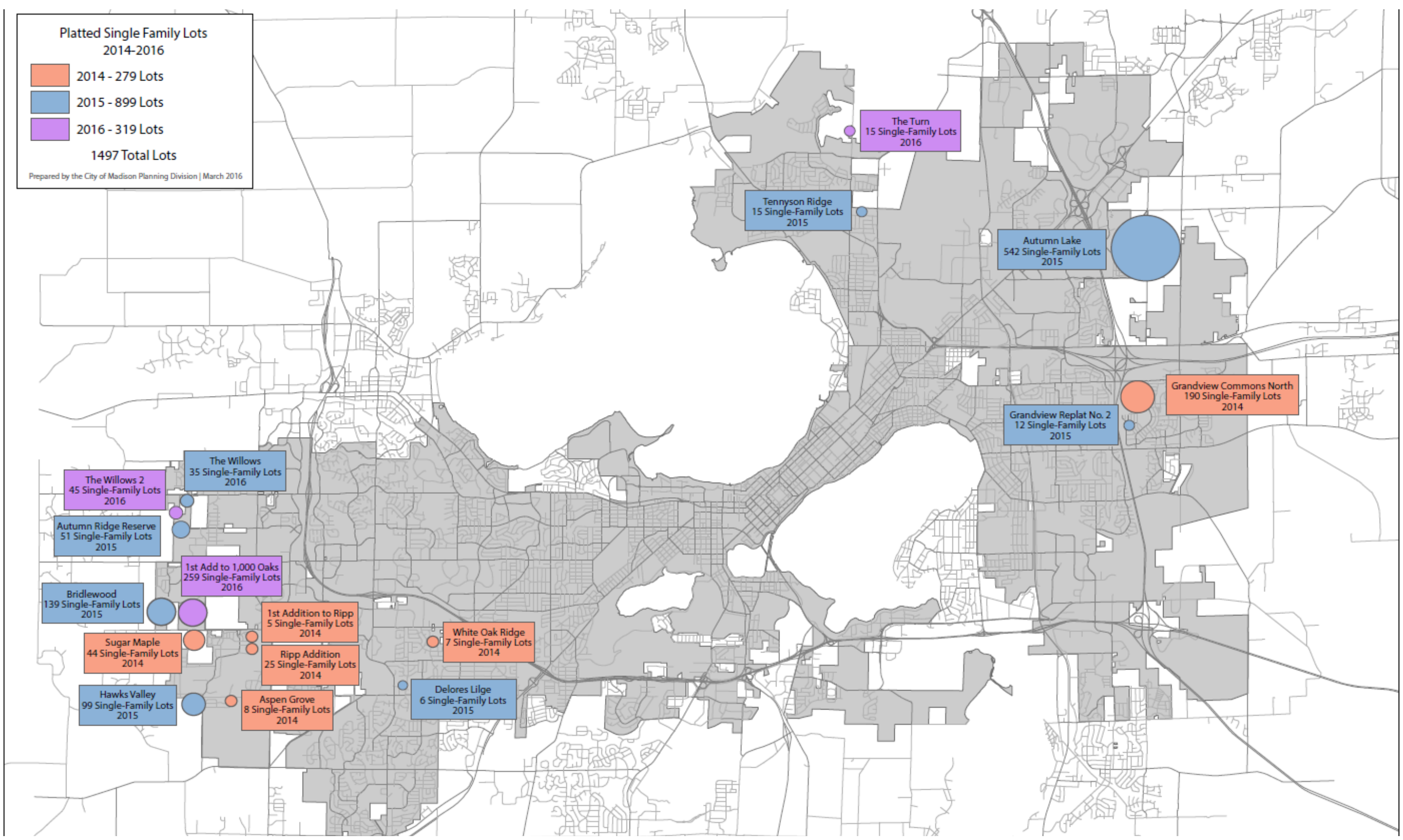
NEW SUPPLY

The City of Madison avoided many of the excesses of the housing bubble of the 2000's and single-family housing construction peaked years before the rest of the county. However, construction has also been slower to recover, with permits in the City essentially flat since 2008, while Dane County started recovering in 2012.



Source: Census Building Permits Survey

Since 2014, roughly 500 new single-family lots have been platted per year. For comparison, 1,000 new homes were built per year as recently as 2003 and 2,661 existing homes were sold in Madison in 2015. Naturally, these newly platted subdivisions are overwhelmingly concentrated on the far east and far west sides of the city.



TRENDS

- Ownership is still relatively affordable in historic terms
    - Low interest rates
    - Recession related price drop
- Very little new supply is being currently being added
- "Opportunity Neighborhoods" are struggling to attract buyers and recover their value
    - Moderate to high percentage of owner occupied homes
    - 40+ year old housing stock
    - Average property value below the City average
    - Longer than average days on market
    - Flat or declining assessed values
    - Located between more central urban/walkable neighborhoods and newer development

MARKET RATE OWNERSHIP - FINANCE/FUNDING

NATIONAL

The majority of funding for ownership housing is in the form of traditional mortgages and owner equity. Virtually all owner occupied housing in the United States is subsidized by the federal government through the tax code and mortgage markets.

- Fannie Mae
    - Offers securitized debt products to the single family home market
    - Sets the market standard for mortgage products at 30 year fixed loans with no prepayment penalty, which might not exist without government support
    - Goal of reducing interest rates and increasing housing supply through providing stability and liquidity to the single family loan market
- FHA Loans
    - The Federal Housing Administration (FHA) provides mortgage insurance on loans made by FHA-approved lenders
    - Allows for lower down payments without the need for private mortgage insurance

LOCAL SOURCES

The majority of local home ownership programs are targeted at households with incomes below 80% of AMI. Madison has three programs with higher income limits:

- Home Buyer's Assistance
    - Combined Down Payment and Rehabilitation Assistance
    - Deferred or installment loan
    - Up to $40,000 with an additional $10,000/unit
    - Averages 6 loans/year
    - Income restricted to $101,125
    - City funds
- Small Cap TIF
    - Combined Down Payment and Rehabilitation Assistance
    - Forgivable loan
    - Up to $80,000 with an addition $10,000/ unit
    - Averages 10 loans/year
    - Geographically restricted to relevant TID
    - Not income restricted
    - TIF funds
- Installment Loan
    - Rehabilitation Assistance
    - Installment loan
    - Up to $19,000 with an additional $3,000 for each housing unit
    - Averages 11 loans/year
    - Income restricted to $129,250
    - City funds

MARKET RATE OWNERSHIP - CHALLENGES

The greatest challenge currently facing our ownership housing market is the loss of middle class of homeowners and lack of new entrants to our homeownership market. There are currently a number of barriers preventing the next generation of homebuyers from purchasing their first home in Madison including:

- Tightened federal mortgage underwriting standards
  - Student debt burden
    - Reduced borrowing capacity because of debt-to-income ratio
    - Lack of downpayment
    - Lower credit score
- Lack of Starter and Mainstream Homes in Central Neighborhoods
- Opportunity Neighborhoods with large amounts of Starter Homes lack amenities that Millennials are looking for

TIGHTENED FEDERAL MORTGAGE UNDERWRITING STANDARDS

As a result of the housing led recession and foreclosure crisis, the newly formed Consumer Financial Protection Bureau (CFPB) created a new set of banking rules designed to make safer loans by prohibiting or limiting certain high-risk products and features with a goal of reducing a borrower's risk of being housing cost burdened or facing foreclosure. The primary rules define a "qualified mortgage" (QM). Lenders that make QM loans will receive some degree of legal protection against borrower lawsuit. Key features include:

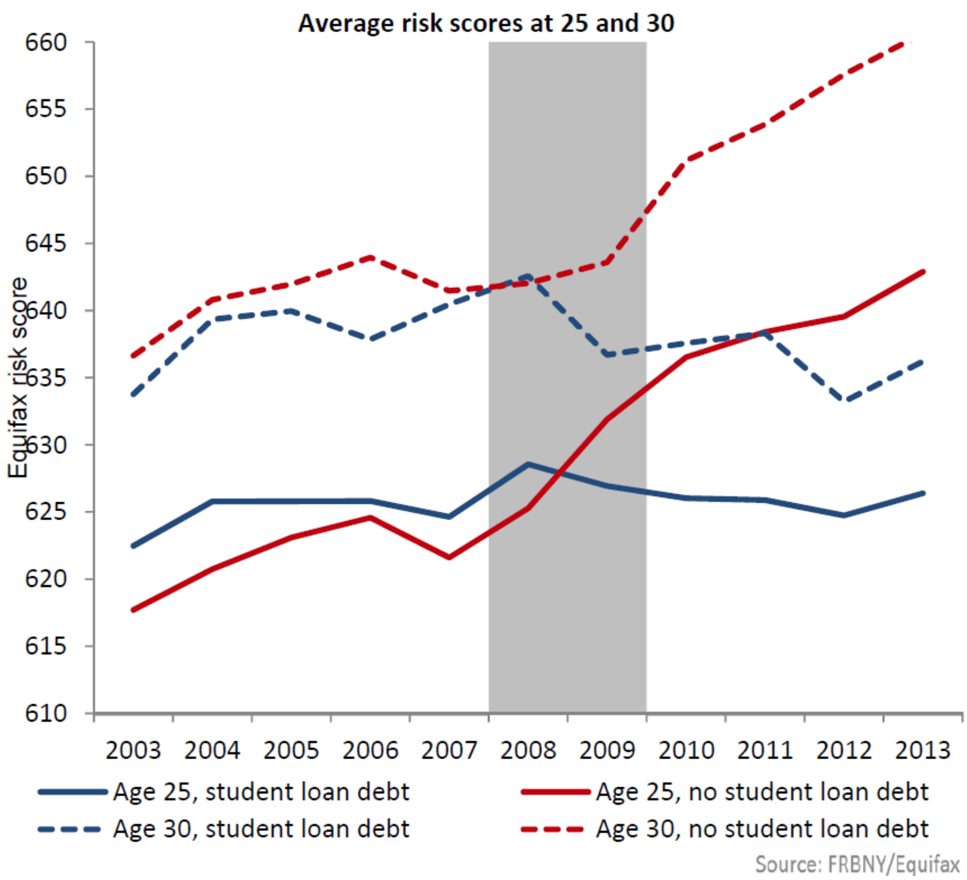
- **No Excessive Upfront Points and Fees**
- **No Toxic Loan Features**
  - ELIMINATE INTEREST-ONLY LOANS
    - These are mortgage products where the borrower defers the repayment of principal and pays only the interest, usually for a certain period of time.
  - ELIMINATE NEGATIVE-AMORTIZATION LOANS
    - These are loans where the principal amount borrowed increases over time, even while monthly payments are being made. This often happens as the result of the interest-only payments mentioned above.
  - NO TERMS BEYOND 30 YEARS
    - In order to meet the definition of a qualified mortgage, the loan must have a repayment term of 30 years or less.
  - ELIMINATE BALLOON LOANS
    - In most cases, balloon loans will be prohibited by the QM rules, a balloon mortgage is one that has a larger-than-normal payment at the end of the repayment term.
- **Limits on Debt-to-Income Ratios**
  - In general, the qualified mortgage will be granted to borrowers with debt-to-income / DTI ratios no higher than 43%. As the name implies, the debt-to-income ratio compares the amount of money a person earns each month (gross monthly income) to the amount he or she spends on recurring debt obligations. This aspect of the QM rule is intended to prevent consumers from taking on mortgage loans they cannot realistically afford.
  - A temporary (after January 2014) exception will be granted for loans that are eligible to be sold or insured by Freddie Mac, Fannie Mae, FHA or the VA.

While these **rules are intended to reduce the risk of housing cost burden and foreclosure, the other result of these rules is that QM mortgages require borrower to have larger downpayments and higher incomes** to get a loan than before.

The alternative for borrowers is to obtain a loan that is kept in-house by the lender (rather than being sold on the secondary market after issuance). These loan products often have higher interest rate and income restrictions in exchange for reduced downpayment requirements.

DEBT BURDEN

Related to stricter underwriting criteria regarding debt to income ratios is the fact that **25-30 year olds have record levels of student debt, which can reduce the size of the mortgage they qualify for and limits their ability to save for downpayments**. In Wisconsin, the average college student graduates with over $28,000 in student loans. (National Center for Education Statistics)



It is not clear if this rise in student debt has significantly reduced borrowers' ability to purchase home, because despite a drop in mortgage originations overall, 25-30 year olds with significant student debt burdens are more likely to purchase a home than their peers without student debt. However, **the data are clear that students with student loan debt have measurably lower credit scores**.

LACK MAINSTREAM OWNERSHIP HOUSING IN CENTRAL NEIGHBORHOODS

As a city, Madison is gaining a significant number upper-middle income households ($100,000-$150,000) that are choosing to rent rather than own. This group would normally comprise the core of the home buying market. Using standard measures of affordability, these groups would be likely purchasers of Mainstream Homes priced at $200,000 to $300,000. The options for Mainstream ($200,000-$300,000) product have been generally limited to three categories:

- Older homes and rental properties that need significant improvements but are in Central Neighborhoods
- Post WWII homes that may need some updating located in Opportunity Neighborhoods
- Newer homes that are move-in ready but are located on the City Periphery

As a result of the housing market crash, a significant portion of our single family homebuilders left the market or retreated to the still profitable high-end of the market. New construction of Mainstream housing products that has returned has been limited to single-family homes along the periphery of the City. New construction of owner occupied housing in more centrally located neighborhoods is rare due to a lending market that does not support condominiums and a regulatory/development community struggles with middle scale/density product types (town houses, small lots/court houses).

The data locally and nationally show that Millennials are more interested than previous generation in living in neighborhoods that provide convenient commutes, alternative transportation, and abundant amenities. Unfortunately, those places tend to be in Madison's more expensive Central Neighborhoods, pricing them out of owning there.

OPPORTUNITY NEIGHBORHOODS

Where Madison has a large supply of moderately priced Starter Homes is in "Opportunity Neighborhoods" which are areas defined by:

- Moderate to high percentage of owner occupied homes
- 40+ year old housing stock
- Average property value below the City average
- Longer than average days on market
- Flat or declining assessed values
- Located between more central urban/walkable neighborhoods and newer development

These areas are generally located in neighborhoods outside of the city core. These areas in general do not have as robust access to alternative transportation and abundant amenities as our more Central Neighborhoods, which is what new buyers indicate they value.

LOCAL MODELS

- Small Cap TIF
    - Program to encourage the rehabilitation and conversion of old rental housing back to ownership
    - Combined Down Payment and Rehabilitation Assistance
    - Forgivable loan
    - Up to $80,000 with an addition $10,000/ unit
    - Geographically restricted to relevant TID
    - Typically located in Central Neighborhoods
    - Not income restricted
    - Utilizes TIF funds
- Mosaic Ridge
    - City of Madison CDA development to encourage owner occupancy in a challenged neighborhood
    - Demolished rental housing and replaced it with single family owner-occupied housing
    - Mixed income goal of 1/3 market rate, 1/3 under 80% AMI, 1/3 under 50% AMI
    - Targeted downpayment assistance to low income buyers

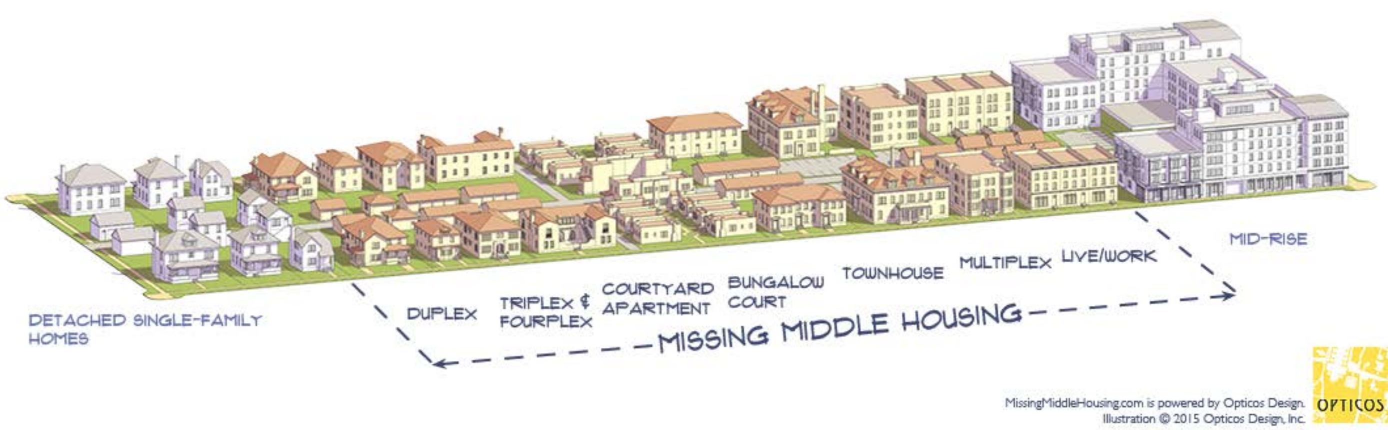
ALTERNATIVE OWNERSHIP MODELS

- Condominiums
    - A form of property ownership where a specified part of a piece of real estate is individually owned. Individual home ownership within a condominium is construed as ownership of only the air space confining the boundaries of the home. Use of and access to common facilities such as hallways, heating system, elevators, and exterior areas are executed under legal rights associated with the individual ownership. These rights are controlled by the association of owners.
    - Individuals purchase units in a process similar to single-family homes
        - Recent rule changes at FHA have made financing more difficult
    - Provides affordability through shared use of common facilities and shared activities to reduce housing and living costs
    - Can be in the form of a single multifamily building or clustered single-family buildings
    - Can be newly constructed or converted from existing rental properties
    - Common area maintenance is paid for by the association of owners which collects dues from individual owners
        - Dues can be large, negating any potential savings from sharing common areas
        - Can be difficult to obtain debt financing for common area repairs if a condo association is underperforming or has dues delinquencies
- Co-housing
    - Multifamily housing composed of private homes supplemented by shared facilities
    - Can be in the form of a single multifamily building or clustered single-family buildings
    - Provides affordability through shared use of common facilities and shared activities to reduce housing and living costs
        - Common facilities may include a kitchen, dining room, laundry, childcare facilities, offices, internet access, guest rooms, and recreational features
        - Shared activities may include cooking, dining, child care, gardening, and governance of the community
    - Can take three legal forms of real estate ownership:
        - Individually titled houses with common areas owned by a homeowner association, condominiums, or a housing cooperative
        - Condo ownership is most common
- Land Trust
    - An agreement whereby one party agrees to hold ownership of a piece of real property for the benefit of another party
    - Can be used to create a program where an entity owns the land (trustee) and rents it to a household that owns the improvement that sits on the land (house)
    - Provides affordability by separating the cost of land (held by a trustee) from the cost of the improvements (house)
    - Ex. Madison Area Land Trust Homeownership Program funded by the City of Madison retains ownership of the underlying land and sells the improvement (house) to qualified homebuyers

“MISSING MIDDLE” PRODUCT TYPES

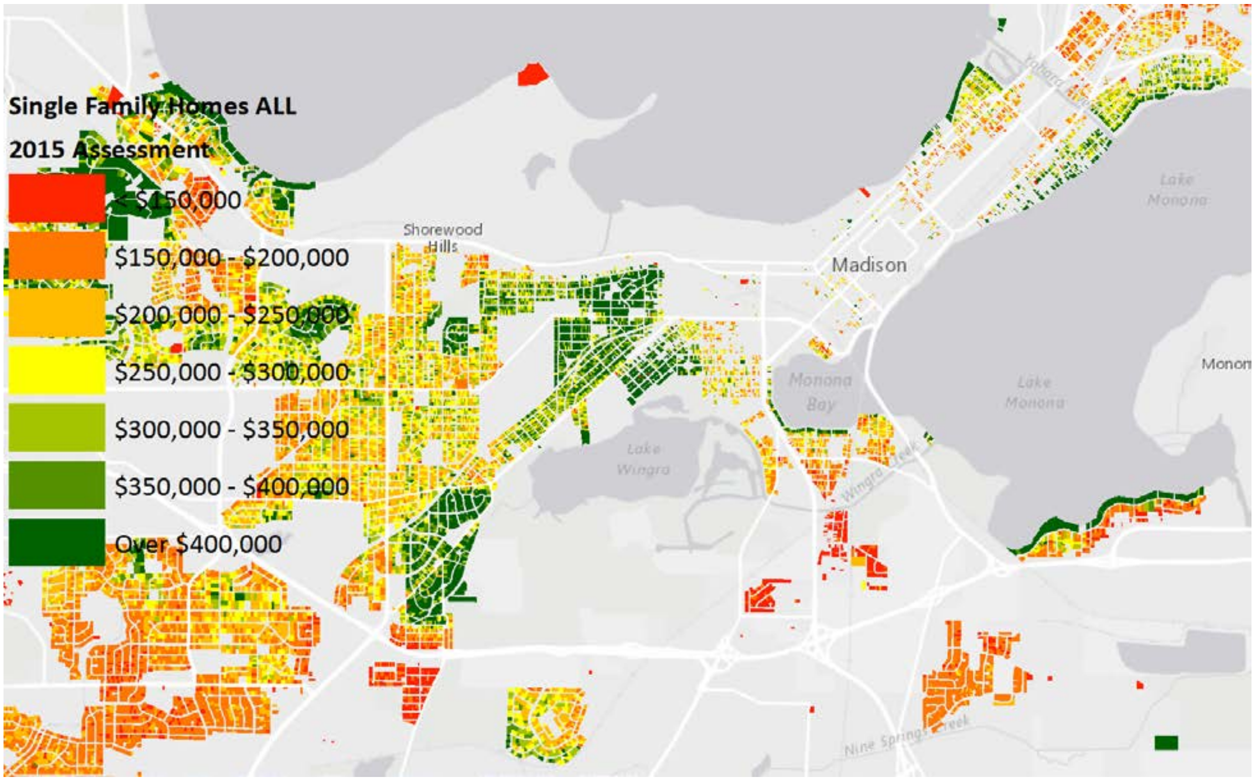
Between detached single-family homes and mid-rise condominium buildings there are a variety of “middle scale” building types that offer the cost savings of efficient construction and density while maintaining neighborhood appropriate size. In Madison, this has typically taken the form of duplexes, but other forms include courts, townhouses and accessory dwelling units. These housing forms are less common in part because of zoning and subdivision rules that prohibit their development. The City of Portland Residential Infill Project serves as a model for systematically reviewing their zoning and subdivision rules to remove barriers to these alternate forms of housing.

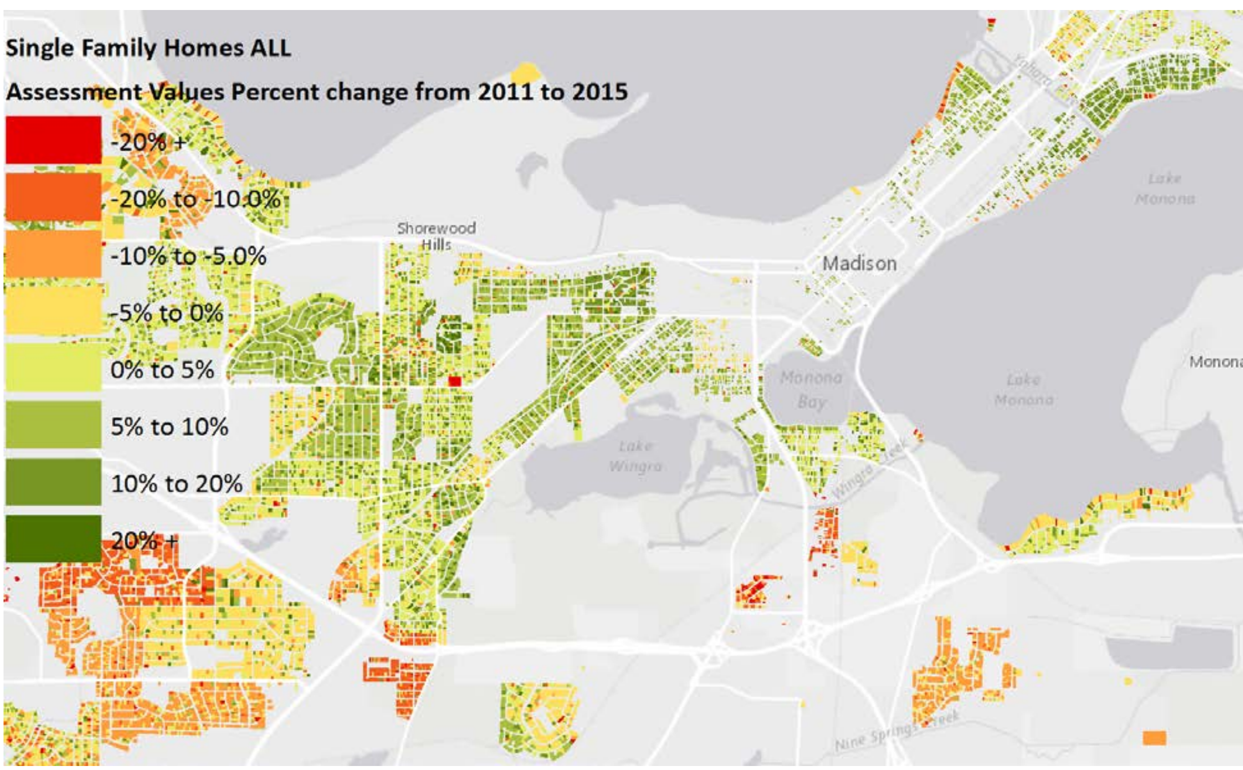
- Small Lots/ Cottage Courts/ Flag lots
  - Zoning Code/Subdivision changes that allow for very small and/or irregular lots to reduce per unit land costs
  - Allows construction of fee-simple, infill housing on small lots with compact building footprints and minimal street front and setback requirements
  - Avoids costs and funding challenges of condominium structures
  - Existing large residential lots can be subdivided to provide smaller more affordable lots
    - E.g. A house on 10,000 sqft single family lot valued at $240,000 can be divided into three lots sold at $80,000
  - Madison currently allows some of these configurations, however they often require rule exemptions
  - E.g. The Los Angeles Small Lot Subdivision Ordinance reduced minimum lot size from 5,000 to 600 square feet and shrinking mandatory setbacks to encourage new housing for “professionals seeking an urban lifestyle in a walkable neighborhood” while maintaining affordability
- Attached Housing/Townhouses
  - A row of identical or mirror-image houses share side walls allowing for smaller lots and construction efficiencies to reduce cost
  - Often owned as a condominium but can be fee simple ownership (usually required a small gap between buildings)
  - Existing large residential lots can be subdivided to provide smaller more affordable lots
    - E.g. A house on 10,000 sqft single family lot valued at $240,000 can be divided into eight lots sold at $30,000
  - E.g. Portland, OR Residential Infill Project
- Micro Housing Units
  - Very small houses or condos, often 100-300 square feet, designed to house single adults or small families
  - The small size allows developers to build units in markets with high housing costs at a lower cost than traditional homes
  - Difficult to build as single family homes in Madison because of the need to meet the requirements of the building code related to energy efficiency, electrical, HVAC, and plumbing (not minimum square footage requirements)

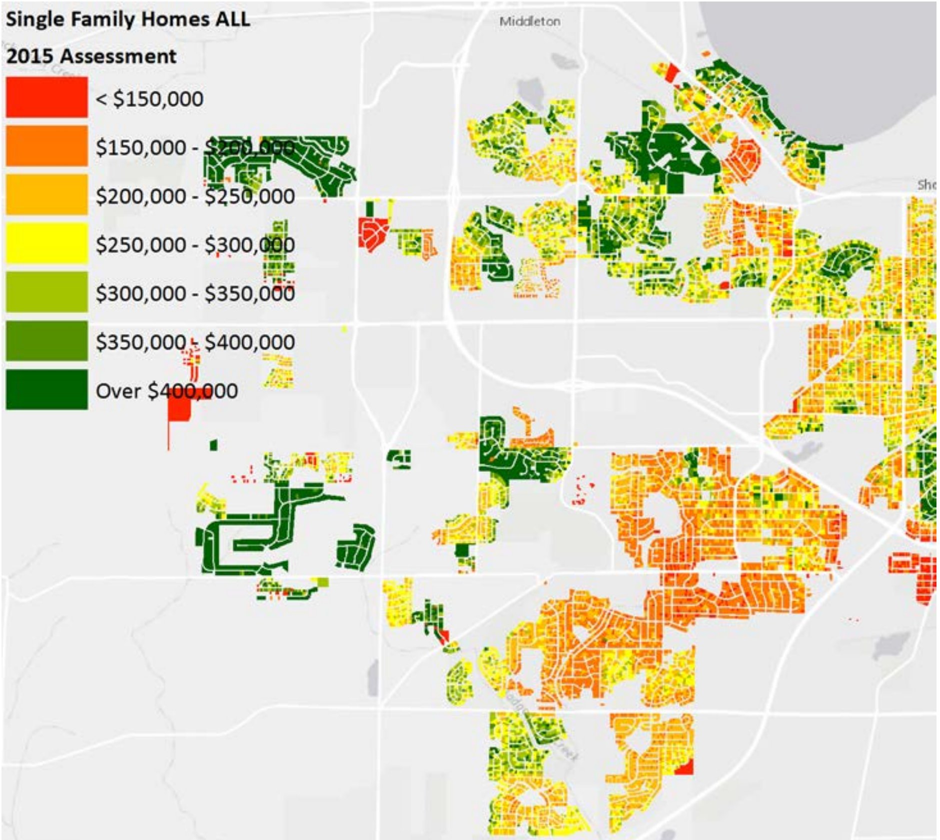


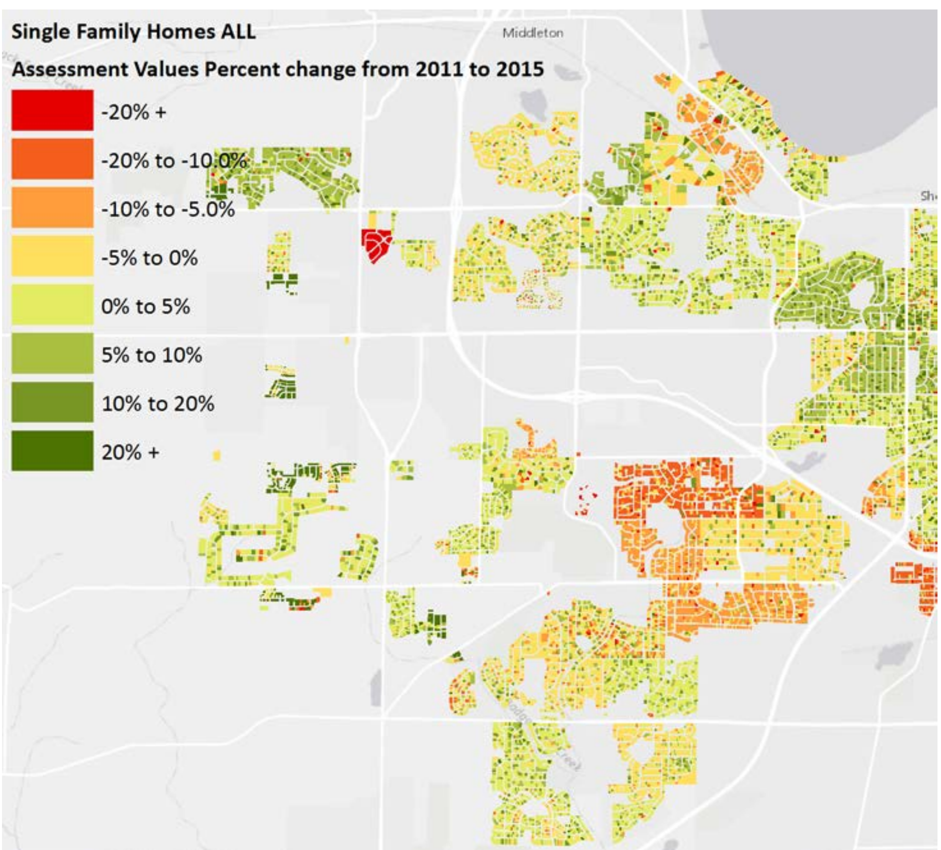
- Exterior Renovation Programs
    - Subsidizes limited exterior renovations to improve neighborhood perception
    - Usually very targeted areas
    - Structured as a matching grant or low interest loan
    - E.g. PAINT Youngstown offers free exterior house painting in targeted neighborhoods on priority streets of Youngstown, OH through the Youngstown Neighborhood Development Corporation
    - E.g. Paint-Up, Fix Up in Westminster, MD provides matching funds for exterior beautification projects in target neighborhoods
- Down Payment Assistance
    - Communities can create programs to subsidize all or part of the down payment necessary for a household to qualify for a mortgage
    - Often funded by federal CDBG or HOME funds
    - Often awarded as a second mortgage that is deferred or gradually forgiven
    - E.g. City of Madison Home-Buy the American Dream, Federal Home Loan Bank Down Payment Plus
- Subsidized Mortgages
    - Local governments can offer mortgage products tailored to low-income populations by offering lower interest rates and fees or relaxed underwriting criteria
    - The Wisconsin Housing and Economic Development Agency (WHEDA) offers low interest fixed rate mortgages through partner lenders for low income homebuyers
- Subsidized Acquisition/Rehab Loans
    - Combination Acquisition/Rehab loans allow buyers to use part of the funds for downpayment with remainder paying for renovations
    - Has the advantage of allowing homebuyers to purchase lower priced homes in need of improvement
    - E.g. City of Madison Homebuyers Assistance (HBA), Small Cap TIF
- Subsidized Rehabilitation Loans
    - Communities can create programs to subsidize all or part of the cost necessary for a household to rehabilitate a home
    - Focused on existing low-income homeowners with limited capital or access to financing
    - Programs typically focus on improvements to achieve building code compliance and energy efficiency
    - Often funded by federal CDBG or HOME funds
    - Often awarded as a second mortgage that is deferred or gradually forgiven
    - E.g. City of Madison Deferred Payment Loan, Installment Loan, Green Madison

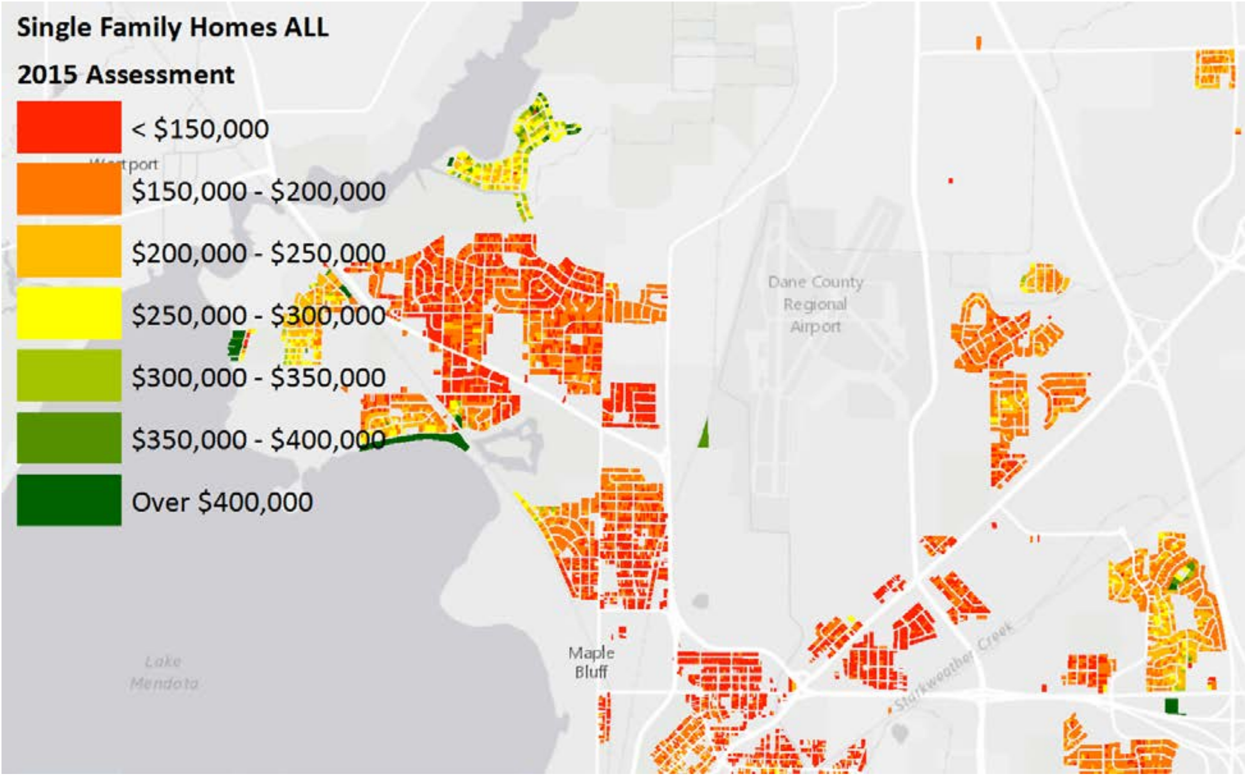
CENTRAL – NEAR EAST – NEAR WEST - SOUTH

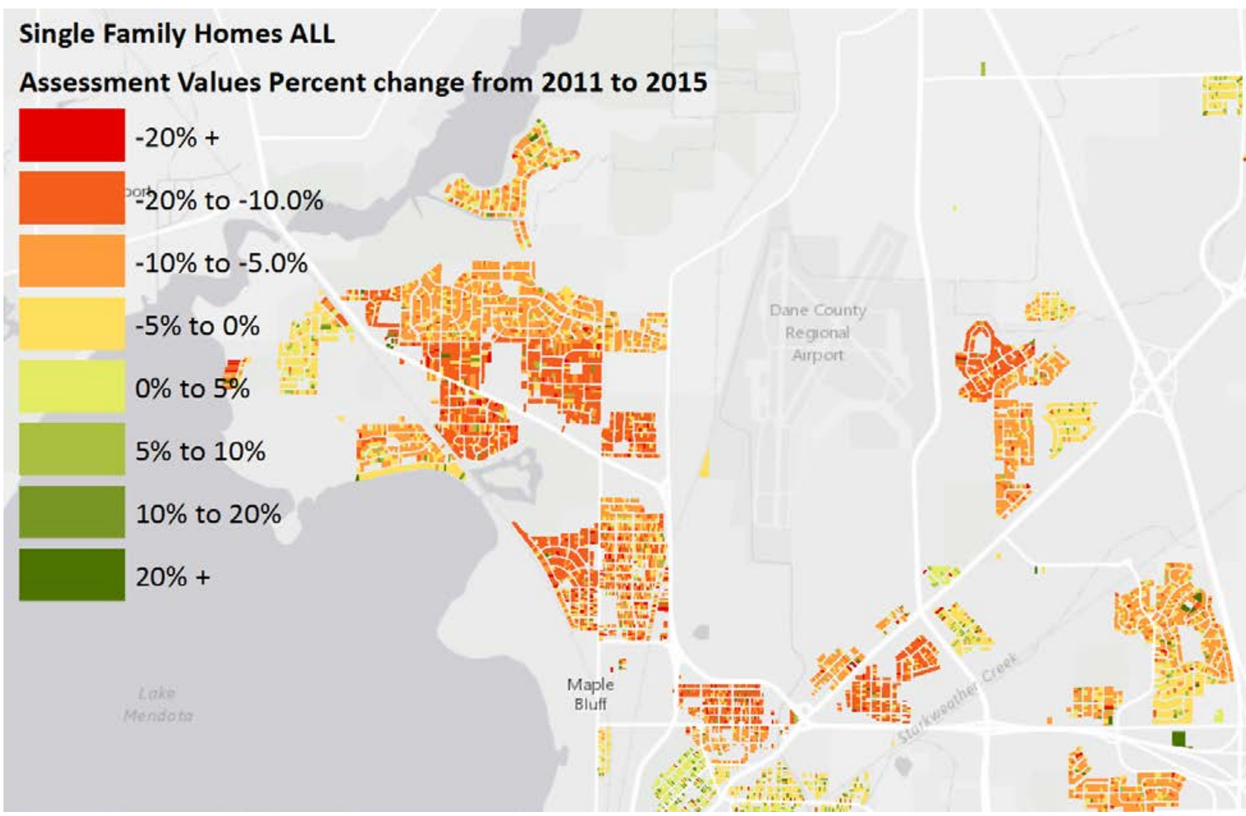


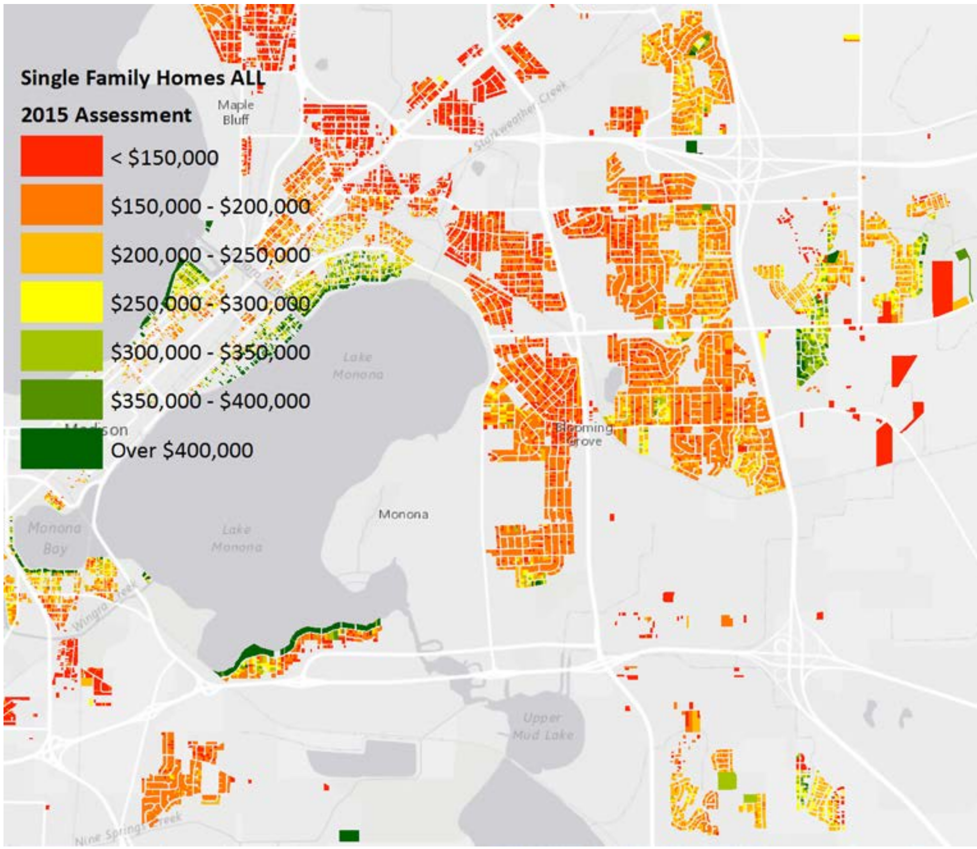


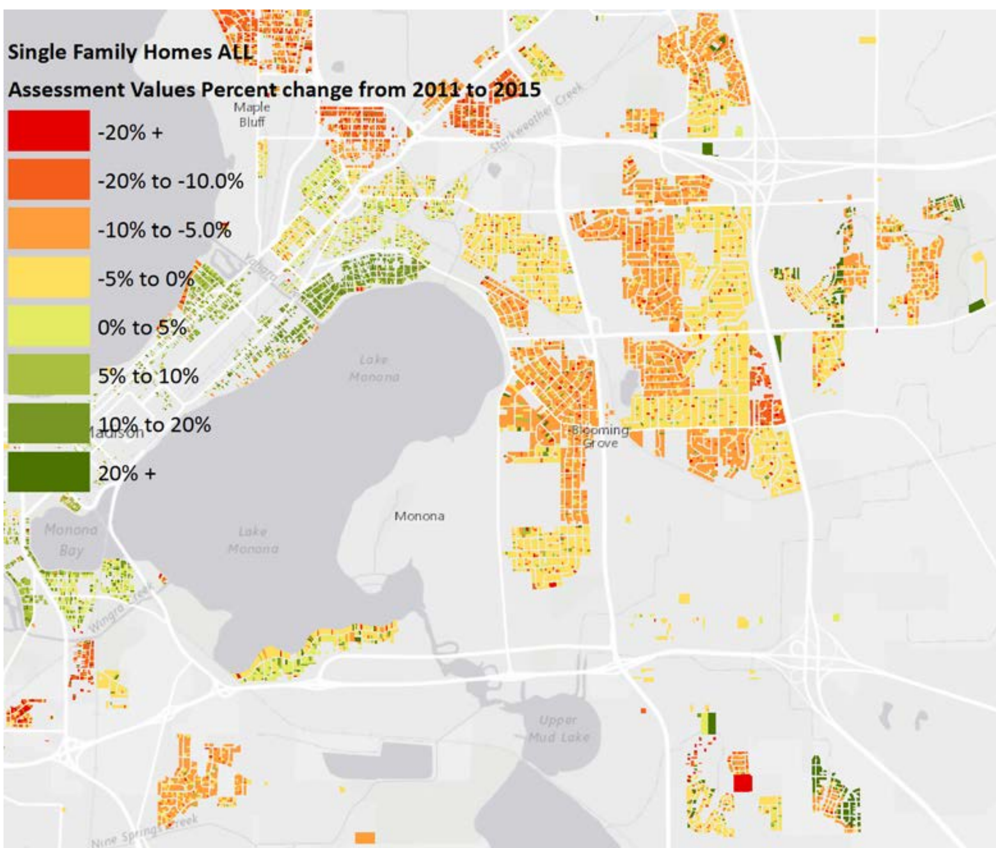

Single Family Homes ALL
2015 Assessment
< $150,000
$150,000 - $200,000
$200,000 - $250,000
$250,000 - $300,000
$300,000 - $350,000
$350,000 - $400,000
Over $400,000
Middleton


Single Family Homes ALL
Assessment Values Percent change from 2011 to 2015
-20% +
-20% to -10.0%
-10% to -5.0%
-5% to 0%
0% to 5%
5% to 10%
10% to 20%
20% +
Middleton


Single Family Homes ALL
2015 Assessment
< $150,000
$150,000 - $200,000
$200,000 - $250,000
$250,000 - $300,000
$300,000 - $350,000
$350,000 - $400,000
Over $400,000
Dane County Regional Airport
Maple Bluff
Lake Mendota
Starkweather Creek


Single Family Homes ALL
Assessment Values Percent change from 2011 to 2015
-20% +
-20% to -10.0%
-10% to -5.0%
-5% to 0%
0% to 5%
5% to 10%
10% to 20%
20% +
Dane County Regional Airport
Maple Bluff
Lake Mendota
Starkweather Creek


Single Family Homes ALL
2015 Assessment
< $150,000
$150,000 - $200,000
$200,000 - $250,000
$250,000 - $300,000
$300,000 - $350,000
$350,000 - $400,000
Over $400,000
Maple Bluff
Lake Monona
Monona Bay
Monona
Blooming Grove
Upper Mud Lake
Starkweather Creek
Nine Springs Creek


Single Family Homes ALL
Assessment Values Percent change from 2011 to 2015
-20% +
-20% to -10.0%
-10% to -5.0%
-5% to 0%
0% to 5%
5% to 10%
10% to 20%
20% +
Maple Bluff
Lake Monona
Monona Bay
Monona
Blooming Grove
Upper Mud Lake
Starkweather Creek
Nine Springs Creek