How does homeownership contribute to wealth building?

Low-income households and households of color have limited access to homeownership because of barriers such as limited supply of affordable housing, restricted access to credit, and systemic inequities. For those low-income households and households of color, homeownership can be a catalyst to wealth building. Home equity accounts for over half their net wealth, but these gains from homeownership vary by income, gender and race/ethnicity.

This evidence brief:

- Summarizes research on the key factors to wealth building through homeownership for low-income households, households headed by single women, and Black and Hispanic/Latinx households.
- Shares how Habitat for Humanity contributes to these factors to encourage wealth building.

EVIDENCE BRIEF

Financial benefits of homeownership for low-income households

Overall, homeownership promotes wealth building by acting as a forced savings mechanism and through home value appreciation. Homeowners make monthly payments that increase their equity in their homes by paying down the principal balance of their mortgage. Home value appreciation also helps homeowners build wealth by enabling them to realize greater proceeds if they sell the home or borrow against the additional equity. In addition, owning a home promotes intergenerational homeownership and wealth building. Children of homeowners transition to homeownership earlier – lengthening the period over which they can accumulate wealth – and have homeownership rates 25 percentage points higher than the rate of children of renters.[1,2]

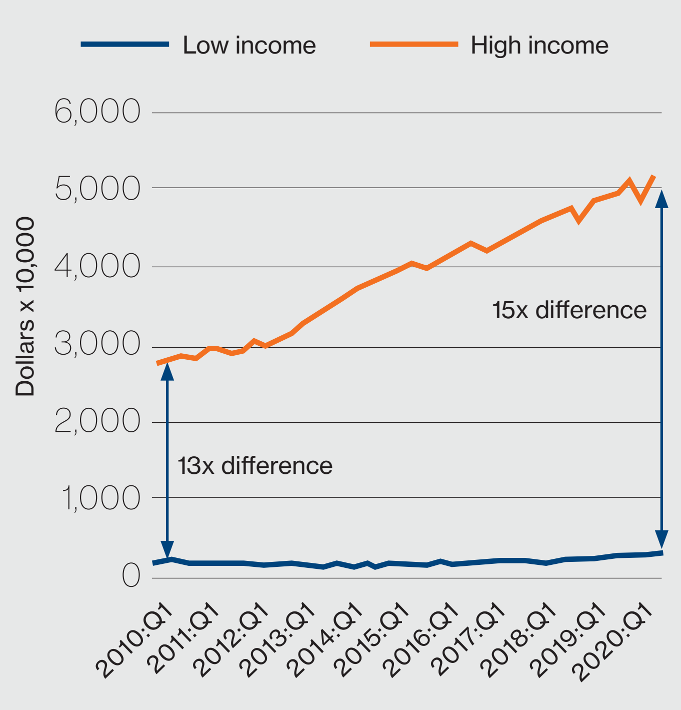
For every dollar in net wealth accumulated by a high-income household, a low-income household amasses 7 cents. This wealth gap has significantly widened over the past decade (Figure 1).[3] Homeownership is a substantial contributor to the wealth of low-income households, since they hold the majority of their wealth in their homes. But do low-income households achieve greater financial returns through homeownership than through renting? Low-income homeowners with sustained ownership and affordable loans have higher wealth accumulation – both housing and non-housing wealth – than comparable renters.[4] Furthermore, low-income homeowners earned higher financial returns than high-income homeowners when the annual costs and benefits of homeownership, which include imputed rents (the rental value that the homeowner would get from renting their home at the market rate), are estimated.[5] The ratio of imputed rents to home values declines with income level and drives this result. The rate of return, however, hinges on the value of imputed rent and the homeowners' ability to build home equity.

Key factors to build home equity

Providing affordable financing and refinancing loans at lower interest rates help low-income households to build equity in their homes.

- Low interest rates reduce the cost of financing and enable homebuyers to contribute more of their monthly mortgage payments to principal – and equity-building – than to interest payments.
- Increasing the initial mortgage interest rate by 1 percentage point increases the probability of exiting homeownership by 16%.[6]
- Low-income households are more vulnerable to predatory lending that lowers home equity through fees, poor underwriting and high penalties. Interest rates for subprime loans can be more than 4 percentage points higher than traditional loans.[7]
- Low-income households are less likely to refinance their existing mortgage to take advantage of lower interest rates. Failing to refinance reduced their aggregate wealth by $22 billion.[8]

FIGURE 1: DISTRIBUTION OF HOUSEHOLD WEALTH FOR LOW- AND HIGH-INCOME HOUSEHOLDS



Sustaining homeownership allows homebuyers to recoup the transaction costs associated with the purchase of a home and to weather home value fluctuations.

- Transaction costs to buy and sell a home can average 8% to 10% of the value of a home.[9] Homeowners can offset the transaction costs by remaining in their homes long enough for home values to appreciate to cover those costs.
- Living in the home for a longer duration also allows homeowners to weather short-term fluctuations in home values and realize positive financial returns.[10]
- Low-income households tend to pay a higher share of their monthly income for housing than do higher-income households, and they have less savings to cushion unexpected financial events such as a job loss or health bills. For low-income homeowners, a loss in income increases the probability that they will transition to renting by 74%.[11] Within five years of buying their first home, over half of low-income homeowners return to renting, compared with 25%-30% of high-income buyers.[6,12]

Appreciating home values increases the equity in the home, especially at the time of resale, but the rate of appreciation depends on the timing and location of the home purchase.

- There is mixed evidence regarding whether lower-priced homes, the type of homes typically purchased by low-income homebuyers, have lower rates of appreciation than higher-priced homes. The level of appreciation depends on the specific period and market.[9]
- Low-income households that purchase during periods of high home appreciation are more likely to realize wealth accumulation than renters, but the reverse holds true during periods of lower appreciation.[13]

How Habitat contributes

- Habitat affiliates help homeowners build equity by keeping the cost of homeownership affordable for low-income families so that homeowners can begin to accrue equity immediately. Habitat is committed to ensuring mortgage payments consume no more than 30% of a homeowner's income and meets this goal by offering financial packages composed of low- or zero-interest loans and forgivable loans. These creative financing packages also help sustain homeownership by providing flexible mortgage restructuring options and other financial support to homeowners when they lose income.
- Habitat also offers down payment assistance that helps people access homeownership earlier and begin accruing equity sooner, granting them more financial resilience and the ability to focus on other financial goals.
- Habitat builds modest homes and manages the cost of land acquisition, development and construction to keep the overall cost of homes low. Moreover, Habitat lowers transaction costs by eliminating the need for real estate agent and other transaction fees.
- Many Habitat affiliates are leading the way on permanent affordability, using land trust programs and shared-equity models to help growing numbers of families build equity through their homes while ensuring that future homeowners will have the same access to affordable homeownership. These tools help manage expensive land costs and rising home prices to retain affordability while still enabling families to build equity through their homes.
- Habitat affiliates also provide financial education classes and pre- and post-purchase counseling that provide tools and strategies to manage household finances, which can render homeowners better able to continue to meet their mortgage payments and sustain homeownership.
- Habitat's repair programs offer homeowners the opportunity to affordably address acute housing problems and improve the quality of their homes. This allows homeowners to maintain their homes at an affordable cost and continue to build equity through homeownership.
- In addition to the direct services that keep homeownership affordable, Habitat advocates at all levels of government for policies and programs that make affordable homeownership more broadly available and support homeowners in building equity through their homes. Our advocacy work focuses on expanding access to safe, low-interest mortgages; tax credits and saving incentive programs to help low-income families build financial reserves; resources such as housing counseling and short-term mortgage assistance to prevent foreclosure; and policies aimed at reducing regulatory barriers to building affordable homes in appreciating markets.

Financial benefits of homeownership for women

In the past decades, homeownership by single women – regardless of race and ethnicity – has outpaced that of single men. In 2020, single women accounted for 19% of first-time homebuyers, compared with 11% of single men.[14] Single men annually earn returns on their housing investment that are 7.9 percentage points higher – after accounting for financing costs – than the returns earned by single women. This is mostly due to market timing and negotiating ability; single women pay approximately 1%-2% more for comparable properties than single men, and then sell these homes for 2%-3% less. For an average home worth $200,000 held for five years, a 2% difference in purchase and sale price translates to single women losing approximately $1,600 per year relative to single men.[15]

How Habitat contributes

- Habitat homes are priced at fair market value, which is the price of the home if it were sold under prevailing market conditions, and are not subject to the negotiating ability of the homebuyer or any implicit bias or prejudice on the part of their real estate agent.
- Mortgage payments for Habitat homes are kept at 30% of the homeowner's monthly income, independent of home value or financing terms. This model ensures that Habitat homes are affordable regardless of gender and protects women from paying higher costs for their homes.
- Consequently, Habitat homeowners, most of whom are female, do not start their homeownership journey at a deficit and instead are able to begin accruing equity immediately upon purchasing their home.

Financial benefits of homeownership for Black and Hispanic/Latinx households

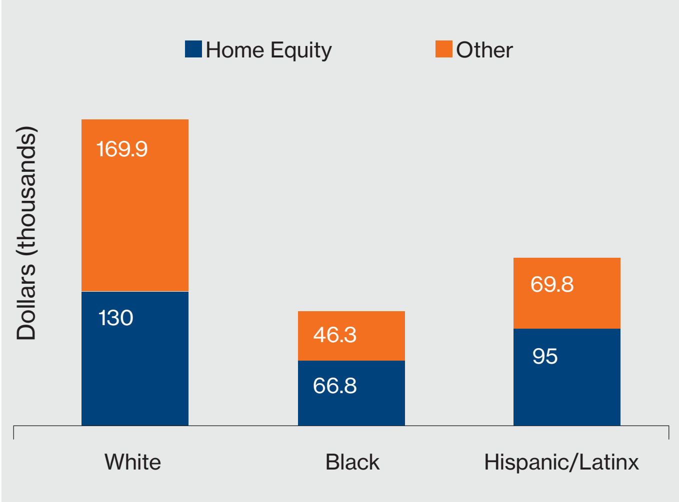
The homeownership rate of white households continues to exceed those of Black and Hispanic/Latinx households, and for Black households, this gap has widened. Black and Hispanic/Latinx households trail white households' overall accumulated wealth and amount of equity amassed in their homes, which is the primary contributor to their net wealth (Figure 2).[16,17] But how do the financial returns of Black and Hispanic/Latinx homebuyers compare with that of white homebuyers? After accounting for the annual costs and benefits of homeownership, Black and Hispanic/Latinx homebuyers – regardless of income level – achieved returns that outpace that of white homebuyers.[5] This result centers on Black and Hispanic/Latinx homebuyers having higher ratios of imputed rent (the rental value that homeowners would get from renting their home at market rates) to home values. However, in addition to the factors discussed earlier, Black and Hispanic/Latinx homebuyers face key barriers that may impact their ability to build equity.

Key barriers to build home equity for Black and Hispanic/Latinx homebuyers

Black and Hispanic/Latinx homebuyers tend to use debt to finance homeownership and face more expensive mortgage financing, paying higher mortgage rates.

- Black and Hispanic/Latinx homeowners are more likely to finance homeownership through debt. The median loan-to-value ratios were 66%, 61% and 56% for Black, Hispanic/Latinx and white homeowners with a mortgage, respectively.[18]
- On average, Black homebuyers pay 29 basis points more than comparable white homebuyers.[19] Financial technology lenders reduce this disparity somewhat, but borrowers of color are still charged interest rates that are typically eight basis points higher than they charge white borrowers with similar financial characteristics.[20]
- During the housing boom of the 2000s, subprime loans were disproportionately concentrated in communities of color, and Black and Hispanic/Latinx borrowers were more likely to receive subprime loans and adverse pricing.[21,22] Subprime lending strips equity, with the excessive fees paid to lenders, contributing to an excessive rate of foreclosures. One in 5 subprime loans end in foreclosure.[23]
- Black homeowners are 16.5% less likely to refinance than white homeowners, and when they do refinance, Black homeowners pay interest rates that are about 1 percentage point higher. This translates to over $22 billion in lost equity to Black homeowners.[7,8]

FIGURE 2: MEDIAN NET WORTH



Homes purchased by Black homebuyers tend to be lower-valued, appreciate more slowly, and have higher property taxes.

- Even after conveying their preferences, homebuyers of color, especially Black homebuyers, are more likely to be steered to disadvantaged neighborhoods by their real estate agents despite having characteristics similar to white buyers.[24] This contributes to households of color tending to purchase homes in residentially segregated neighborhoods that are likely to experience limited or even negative home appreciation.[5]
- In neighborhoods where Black households represent the majority of the population, homes are valued at about half the price of homes in neighborhoods where there are no Black households. Furthermore, similar quality homes located in neighborhoods with similar amenities are worth 23% less in majority Black neighborhoods, compared with those with very few or no Black residents.[25]
- Black and Hispanic/Latinx homeowners also pay higher property taxes than do white homeowners. For every $1 of property taxes paid by white homeowners, Black and Hispanic/Latinx homeowners pay an additional 10 to 13 cents. This is due to the higher tax-assessed values of their homes within similar neighborhood types and the lower likelihood that they will appeal assessments and receive reductions in assessments. This disparity in assessment amounts to an extra $300-$390 annually for the median Black and Hispanic/Latinx homeowner.[26]

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FIGURE 3: BLACK-WHITE GAP IN HOME VALUATION AND PROPERTY TAXES PAID

Black and Hispanic/Latinx households are less likely to sustain homeownership.

- Low-income households of color are slower to transition to ownership, more likely to return to renting, and less likely to return to homeownership if they have transitioned to renting than white households at similar income levels.[12,27] Less than half of low-income homeowners of color remained homeowners within four years of becoming a homeowner, compared with 60% of low-income white homeowners.[12]
- For those able to sustain homeownership through economic decline, Black and Hispanic/Latinx households are more likely to end up with negative equity than comparable white homeowners. For Black households, this is largely driven by the housing market in which they purchased their homes.[28]

How Habitat responds

- Habitat serves a diverse range of homeowners, providing more equitable access to low-cost financing that can help support building home equity. Mortgages for all Habitat homeowners, regardless of race, are priced to be affordable, with monthly payments kept at 30% or less of income, and Habitat affiliates can create unique financing options that meet the needs of all of their homebuyers.
- The counseling and classes offered by Habitat affiliates can help ease the transition to homeownership for low-income households of color and better position them to sustain homeownership.
- Habitat advocates for policies that increase and broaden access to safe and sound credit for underserved populations and help close the homeownership gap for Black households and other communities of color.
- Habitat also advocates for anti-racist housing, lending and land-use policies at the local, state and federal levels that seek to increase racial equity in homeownership.

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285 Peachtree Center Ave. NE, Suite 2700, Atlanta, GA 30303-1220 USA
322 W. Lamar St., Americus, GA 31709-3543 USA
(800) 422-4828 fax (229) 928-8811 publicinfo@habitat.org habitat.org

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