The Socio-Economic Benefit of Home Ownership in Low and Moderate Income Communities

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ABSTRACT

The United States government spends billions of dollars on home ownership programs in low and moderate income communities. However, there is paucity of academic research to assess the socioeconomic impacts of these programs. The purpose of this empirical research was to assess their possible impacts. The key research question explored the relationship between low and moderate income home ownership, the independent variable, and the dependent variables of the rates of crime, unemployment, high school graduation, and standardized test scores in the communities concerned. The research design was quantitative-causal. Welfare economic theory formed the theoretical foundation for the study. Using public records, data were collected from four low and moderate income communities in major Midwestern metropolitan areas. The proposed relationships were tested through independent sample t-tests and regression analyses. Results indicated no significant relationship between low and moderate home ownership rate and the rates of the studied socioeconomic indicators. A significant social change implication of this finding would be to relocate federal dollars from housing schemes to more socially and economically relevant programs, such as those geared toward improving educational opportunities in low and moderate income communities.

DEDICATION

I would like to dedicate this work to my maternal grandparents, Thomas W. and Katherine M. Caven. They were both very hard working people who instilled a great sense of responsibility in me. While my time with them was short, their personal ethics and dedication to their family helped me understand how truly great they were.

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CHAPTER 1:

INTRODUCTION TO THE STUDY

Introduction

Over the past thirty years, the United States Government has played an active role in developing greater home ownership opportunities for low and moderate income families. The government intended to support these opportunities by a combination of regulatory changes and direct program funding to increase the options available to the targeted groups. The government's immediate goal was to improve the funding options for underserved communities; its long-term goal was to improve the overall socio-economic condition of the community.

Although research has examined the socio-economic benefits of home ownership in general, less attention has been given to the benefits of changes in home ownership in low and moderate income communities. Given this lack of attention, the intent of this study was to identify the regulatory and programmatic interventions to understand whether improvements in home ownership occurred, and to assess the socio-economic benefits of those programs in a low and moderate income community.

Given the breadth of government regulations from the Community Reinvestment Act to the Home Mortgage Disclosure Act, the government provided the encouragement to lenders in providing mortgage options that address the needs of low and moderate income communities that were not previously available in the market. Additionally, the government has established several funded programs to provide a financial stimulus to lenders, community groups, and individuals in the effort to support home ownership to the low and moderate income markets.

An additional problem is the inconsistency in available data that would support a relationship between home ownership and accepted socio-economic measurements within low and moderate income communities. Secondly, related to the impact of government regulations and funding efforts, it is proving to be quite difficult to assess the benefits of one particular program or regulation since there is typically a combination of several options that could be used at any point in time. For example, in instances where multiple funding sources used on a single project it could prove difficult to determine whether one source was any more effective than another.

To address these problems, the aim of this study was to study the socio-economic benefit of home ownership in low and moderate income communities. Evidence suggests that the public investment has not always yielded greater community benefit (Czerwinski, 2006). For example, programs such as HOPE VI have intended to spur home ownership in low and moderate income homes, yet the effectiveness of such programs has not been measured. Acts like the Community Reinvestment Act, also intended to encourage home ownership, have also been limited in their effectiveness. Such acts have tended to relax the underwriting standards of banks to get more customers, thereby increasing loan delinquency and foreclosure (Dreier, 2003). Given the disconnect between government initiatives and effectiveness in the community, alternate investment channels may yield better results. For example, research has found a link between educational attainment and general community benefit. These findings suggest that an investment in education may be a more effective alternative to housing that could yield an equal or better benefit for the community.

Statement of the Problem

The United States government has spent billions of dollars in direct financial support and administrative expenses to improve community conditions (Wood, 2007). However, little evidence exists to substantiate the effectiveness of government efforts on home ownership in low and moderate income communities. An initial review of literature revealed that the nature of the relationship between home ownership and socio-economic benefit is unclear. Therefore, the problem is that, while there are benefits that individual home owners may have as a result of these programs and investments, how the change in home ownership has to greater community health remains unclear.

To determine the socio-economic impact of these government programs, I examined the relationship between home ownership (i.e., the non-manipulated independent variable) and crime rate, unemployment rate, high school graduation rate, and high school test scores (i.e., the dependent variables). My intention was to assess housing growth between two low and moderate income communities from the perspective of the ratio of total owners-occupied housing within the total housing available. This ratio identified both the community area with no growth and the community area with high growth. Because the demographic characteristics of the communities were similar, this process of indexing served to reduce any inconsistencies in growth between the community areas.

This information provided an inference as to whether home ownership related to other socio-economic measurements. This information then provided a basis to the larger discussion on welfare economics with specific application to Pareto efficiency whereby any improvement in economic conditions of one individual is not to the detriment of another. In this context, there is not a shifting of wealth from one individual which then allows another individual to purchase a home.

Background of the Problem

The underlying intent of government programs has been to develop greater opportunities for home ownership in the low and moderate income communities. The goal of these efforts was to improve the quality of communities through the increase in home ownership. By increasing home ownership, it was believed, other socio-economic factors would improve, such as a decrease in crime rate and increase high school graduation rates.

Historically, lenders have accepted deposits from the communities they served, only lending to individuals with the least risk of defaulting on a loan. The result of this practice has been that few individuals with a low and moderate income have been able to get loans or establish credit. The majority of loans have been given to individuals earning an upper income. These individuals have also comprised the population that typically owned their own home, thereby leaving the low and moderate income population to either rent or live in less-than-adequate owned housing (Dreier, 2003).

To address this discrepancy in home ownership, the government began implementing regulations to encourage lenders to serve a larger community. Among the most popular regulations was the Community Reinvestment Act of 1977. The primary focus of this act was an improvement to the oversight of lenders that would force lenders to provide credit to a demographic representation of the communities served. From this act, banks would be forced to lend to the same populations from which they had accepted deposits. Banks were also forced to consider the penalties associated with non-compliance with the regulations. For example, non-compliance to the requirements of the Community Reinvestment Act would limit a bank's ability to create and offer new products or even open additional branches in the community, thus stopping any growth efforts until the non-compliance issues were resolved.

Initially, the lenders fought the regulations, arguing that lending to people previously considered non-qualifying may put their business at peril and result in poorer performance to investors. However, the government's regulations passed and were put into law. As a result, the lenders were forced to create new strategies to address the needs of the low and moderate income community.

Along with these new regulations, there was also a need for the government to directly fund programs that would support home ownership in the low and moderate income communities. The government considered the regulations to be an effective first step in the process, the potential market still needed to provide financial incentives to potential home owners, community groups, and lenders. Over time, the government established several different funded efforts such as the HOPE VI program and Bank Enterprise Award program to provide a financial stimulus to a greater population.

The programs did increase home ownership, but little research has measured the community changes from such programs, particularly the socio-economic benefit to low and moderate income communities. Additionally, limited attention has been given to the management of government funds, and little guidance is available for local organizations to report performance back to the government. In the absence of this guidance, some community organizations may use government funding for efforts unrelated to the program goals.

Purpose of the Study

The purpose of the study was to examine the socio-economic changes in home ownership in low and moderate income communities. Historical data were examined, relating to home ownership, crime rate, employment rate, high school graduation rate, median income rates, and academic test scores in two low and moderate income communities in Chicago and two counties in Indiana. Analysis of these variables provided empirical evidence of the socio-economic impact of home ownership on low and moderate income communities.

Theoretical Framework

Arrow (1983) and Sen's (1997) welfare economics theory, and Keynes (1936) and Friedman's (2002) market economic theories were used to define areas of government regulation and distribution of government funds and to study the impact of government funding on community performance.

Welfare economics theory posits that no one individual should become better off at the expense of another individual. Arrow (1983) and Sen's (1997) theories of welfare economics conceive of taxes as a means to equalizing wealth across the population. Taxes could equalize other factors such as educational opportunities, which have been considered by some (Keynes, 1936) as one of the primary environmental factors for equal opportunity. This tenet is commonly referred to as Pareto optimality.

However, a variety of theorists, including Friedman (2002), consider that a typical market economy is not Pareto optimal. The market economy in general contests the idea of Pareto optimality, as there will always be an unequal distribution of wealth. Keynes' (1936) theory on the multiplier effect of money conflicts with Friedman's market theory. For example, Keynes' theory posited that greater funds in a system would correlate with greater consumer spending, which would, in turn, spur improvements in overall income.

Friedman's (2002) theories do not support active regulation or long-term programs to support low and moderate income communities. On the other hand, Keynes' (1936) theory suggests that it would be more effective for the government and the market to invest in this effort. Keynes held the perspective that with the investment the government makes, that investment would result in improved economic conditions for the individuals receiving support from the programs. Arrow (1983) and Sen (1997) considered these housing development programs to be the goals of welfare economics. They saw these programs as providing a greater opportunity for low and moderate income families to improve their financial condition. However, they followed different reasoning compared to Keynes. Arrow and Sen considered government programs to be one of many income distribution programs to provide greater opportunity in the community. Both considered education to be the key vehicle to provide an individual with the ability and the skill to be more professionally productive in their professional lives.

All of these theories were brought into a greater context of the current state of the housing market as well as the performance of programs and regulations developed to support improvements in housing programs in low and moderate income communities. Both welfare and market economics theories were used to determine whether the government efforts resulted in Pareto optimization as well as a resulting socio-economic return on investment.

Assumptions

Given that the purpose was to assess the socio-economic benefits of home ownership in low and moderate income communities, I assumed that the people in this study wanted to own a home and did not want high residential turnover. I also assumed that they wanted to improve themselves socio-economically.

Scope and Delimitations

The study included a socio-economic assessment of a low and moderate income community in the city of Chicago. Two low and moderate income neighborhoods were studied. Although these neighborhoods shared similar demographics, one neighborhood had a history of growth in home ownership whereas the other had limited housing growth. The study focused on two counties with a significant low and moderate income population in order to assess the relationship between owner-occupied housing stock and unemployment.

Variables under study were limited to crime rates, high school graduation rates, rates of home ownership as well as unemployment performance. This information was accessed both from the Federal Government level as well as public information managed by the city of Chicago. The delimitation of the study was that it was not feasible to examine every low and moderate income community in the U.S. Instead, the focus was on the particular neighborhoods or counties discussed above. While these areas were defined as low and moderate income, the delimitation may have an impact on the ability to apply the specific findings to other low and moderate income communities in the United States.

Limitations

The predominant limitation of the study related to data access. Although most of the data were in the public domain, data on the historic high school academic performance were not available. Additionally, the data was limited to two Chicago community areas and two Indiana counties. For example, one of the data points reviewed was the American College Testing Program test scores of high school students in the target neighborhoods. Although the ACT test has been offered as an optional examination for over twenty years, the text was not required in the state of Illinois until the 2000-2001 academic year. Thus, these data only identified the academic performance of students starting high school in 1997 or later.

This study was also limited by the gentrification of neighborhoods over the period under review. From this limitation, outcome measures could reflect the changing dynamics of the neighborhood as well as the city. However, by comparing reasonably similar neighborhoods within the city, the likelihood that similar dynamic changes would affect both neighborhoods in the comparative study was lessened.

Another limitation was that the data related to crime rate only included those crimes that were reported to government authorities. The true number of crimes may have been higher than what was reported.

Furthermore, unemployment related data only reported on those not working and actively seeking employment. This data did not report on those who are unemployed, but not seeking work. This limitation may have resulted in an underreporting of unemployment information. Since unemployment data were not tracked at the census tract level, it was necessary to utilize employment data at the county level in order to provide an assessment of the effect of changes in home ownership. Given that unemployment data were not available at the community area level, I considered median income information at the census tract level as a substitute for unemployment data within the overall community area analysis.

Data were also limited to public students, and did not include private or magnet school students. With this limitation, data were excluded because it was difficult to assess the performance of individual neighborhood residents when their performance was reported along with other students who did not reside in the neighborhoods under study.

This study was also limited by other uncontrollable external factors that could have impacted the performance of any neighborhood. For example, in a generally declining economy, events such as drastic changes in unemployment will deteriorate in most communities but can also have an adverse impact on low and moderate income communities at a higher level which could result in increases in crime and decreases in educational performance. Although these changes may have hindered the generalizability of these findings to different communities, the selection of two community areas within the same city served to mitigate some of these limitations.

Definition of Terms

The following terms will be used throughout the text of this study.

Academic Scorecard: An annual report provided for each public school within the State of Illinois that lists the quantifiable information related to test score performance, graduation rates and overall enrollment at the school, district and state level.

Bank Enterprise Award (BEA): A United States Government funded program that provides financial incentives for banks to support low income housing programs.

Community Development Block Grant (CDBG): A United States Government funded program that provides targeted funding assistance to low and moderate income communities.

Government Sponsored Enterprise (GSE): Financial services corporations established by the United States Government to provide greater access to credit. Fannie Mae and Freddie Mac are considered to be Government Sponsored Enterprises.

Low Income Housing Tax Credit (LIHTC): Provides a federal tax credit to private investors who develop low and moderate income housing programs.

Prairie State Examination: A mandatory standardized test required of all Illinois Public High school students that is completed at the end of the 11^{th} grade. The ACT test is included within this examination.

Nature of Study

This study employed a quantitative design, involving collection and analysis of the existing data regarding the effects of home ownership on certain socio-economic characteristics of low and moderate income communities. Because the existing data were used, a quantitative design was the most appropriate method to use for this research. Secondly, as noted above, while past research may not have focused on this community, the gathered data as well as the analysis methods used were consistent with this research as well.

Research Questions and Hypotheses

For the purposes of this study, indexed changes in home ownership in the low and moderate income community were considered as the non-manipulated independent variable. With that, the following research questions were considered.

1. What is the relationship between home ownership in low and moderate income communities and crime rate?
2. What is the relationship between home ownership in low and moderate income communities and unemployment?
3. What is the relationship between home ownership in low and moderate income communities and standardized test scores?
4. What is the relationship between home ownership in low and moderate income communities and high school graduation?

Other variables within this analysis were considered, such as median income, to address potential external factors impacting the collected data. The inclusion of these variables provided a more ecologically valid understanding of the economic conditions of the selected low and moderate income communities.

Significance of the Study

Although research has illustrated the benefits of government funding on home ownership in general, little attention has been given to the impact of government funding on low and moderate income communities. Thus, while research has supported further public funding of these programs, little research has indicated the impact of those funds on low and moderate income communities.

Many constituencies can benefit from this research. First, the government may use this information to determine whether tax dollars should continue to be invested in improvements to home ownership, and whether existing regulations for greater lending are benefiting banks and communities. Second, the community members may use this information to redirect available funds, identify interventions that could provide better community benefit or to identify a more effective set of regulations that can improve community health.

This research could also benefit those who are seeking to implement community-wide interventions for greater home ownership. This information may lead to the development of different initiatives such mixed-income housing developments or commercial real estate developments within the community to better address negative performance of some of the important socio-economic performance measurements.

Summary

A conflict exists when discussing the perspectives of welfare economics and market economics applied to low and moderate income home ownership programs. There is a desire from the public to assist low and moderate income families in owning a home, it is unclear which stakeholders should facilitate the effort. Market theorists like Friedman (2002) hold that lenders should identify the market and address the demand, whereas welfare economic theorists like Arrow (1983) argue that the government should spearhead the effort. In section 2, I consider a contemporary application of both market and regulatory actions in the low income housing market, grounded in market and economic theories. In chapter 3, I discuss the method used to collect and analyze my data. In chapter 4, I present the results to my analyses for each research question. In chapter 5 I explain the applicability of the study results and suggest recommendations for future research related to this topic.

CHAPTER 2:

LITERATURE REVIEW

Introduction

For the past thirty years, the United States Government has provided additional opportunities for low and moderate income families to own their own home. The government's intent was to address the discriminatory practices by. These steps were driven by the theory that home ownership would also improve other socio-economic aspects of low and moderate income communities.

In this chapter, I will present some of the major regulatory and government-funded programs that have been implemented to meet the needs of the low and moderate income population. I will also discuss the market response from lenders and consumers as well as the impact these efforts have in low and moderate income communities. I will also detail the response from the lending industry both from a compliance perspective as well as the identification of new product options designed specifically for potential low and moderate income home owners. From there, the my focus will turn to reviewing several examples of government funded programs developed to provide financial incentives to lenders and communities to provide further investment in low and moderate income communities throughout the United States. Finally, my review will continue with an application of the general socio-economic community benefits of high home ownership within the general context of welfare economic theory and its applicability to low and moderate income housing programs.