Introduction

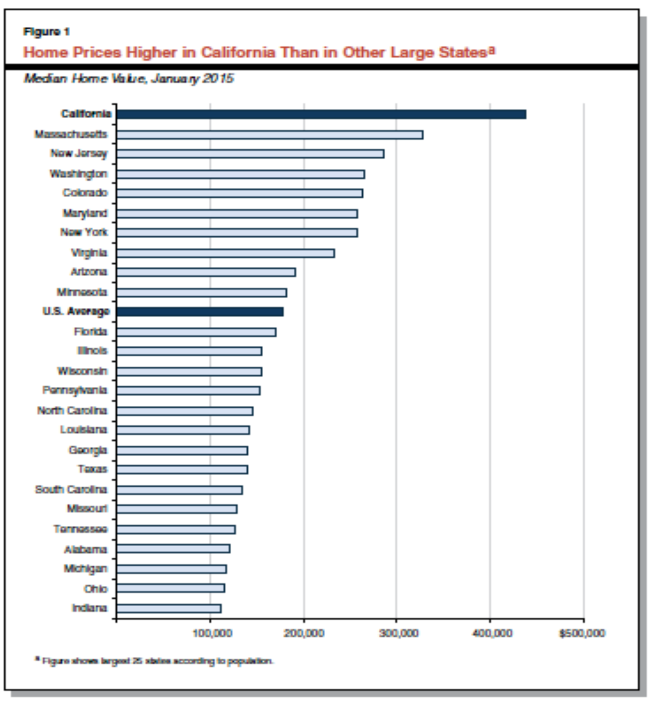
Housing is the most pressing issue facing Los Angeles. Los Angeles suffers from an acute shortage of housing, from houses for middle-income families to three- and four-bedroom apartments for working-class families to studios for young people to single resident occupancy units for very low-income individuals.

For decades, the city has failed to address this issue in a strategic, comprehensive manner, and the result is an enormous problem that impacts millions of residents today, creates growing social problems, and will choke off economic growth in the near future.

There is no question: the most important threat to the social fabric and continued economic growth in Los Angeles is the housing deficit. For LA's future prosperity and the well being of its residents, addressing and solving the housing dilemma is the most urgent task facing the city.

The Problem

The housing crisis is a statewide problem. The California Legislative Analyst Office stated, "The typical California home costs more than double the typical U.S. home and the median monthly rental cost was nearly 50 percent more than the national average."[1] (See Figure 1 from the LAO analysis)



The California story is bad; the Los Angeles story is worse. Zillow pegs the Los Angeles median home price at $610,400—**more than three times higher** than the national median.

Homeownership is so expensive that an increasing percentage of residents have been forced into the rental market. Los Angeles is "the metro area with the highest proportion of renters in the nation at 52 percent."[2] And the cost burden for renters has increased. Severe rent burdens—the ratio of rent to income—have long impacted low-income residents; increasingly, it's now a middle-income problem as well.

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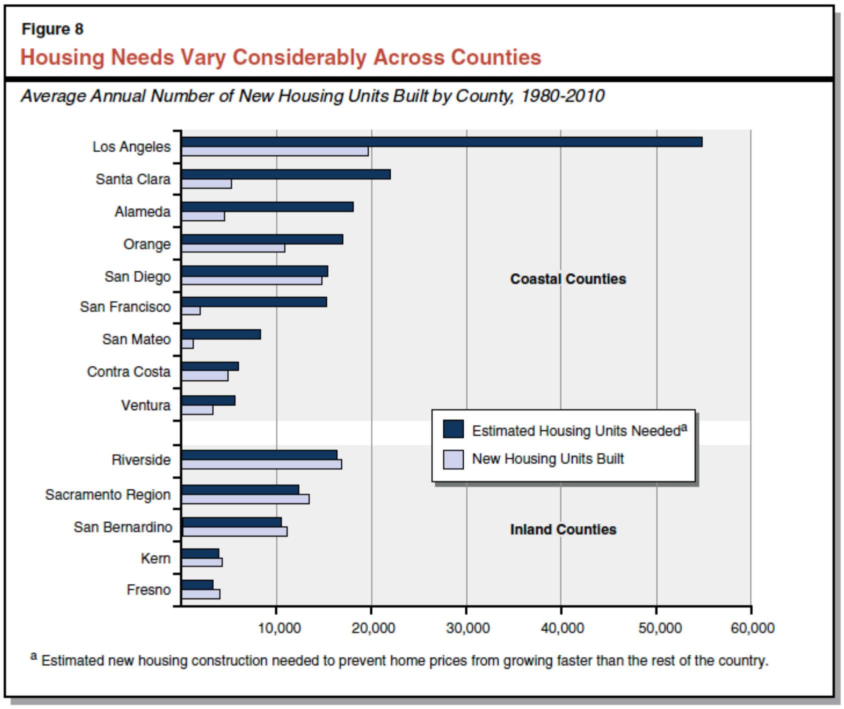
[1] Chas Alamo and Brian Uhler, *California's High Housing Costs: Causes and Consequences,* Legislative Analyst's Office, March 17, 2015, 6.

[2] Rosalie Ray, Paul Ong, and Silvia Jimenez, *Impacts of the Widening Divide: Los Angeles at the Forefront of the Rent Burden Crisis,* Center for the Study of Inequality, UCLA Luskin School of Public Affairs, rev. Sept., 2014, 4.

Origins of the Problem

The high cost of housing—for renters and homeowners—is a simple Economics 101 problem: housing demand exceeds housing supply. From 1980 to 2010, the population in Los Angeles grew 42 percent faster than the number of housing units.[3] The shortfall in the construction of new housing units is statewide, but it is extremely acute in LA. How acute? The housing shortage for low-income renters, for example, is an estimated 382,000 units.[4]



Not only is the City short on housing, its existing stock is old, with more than half built before 1950. The result: Housing in Los Angles has "has a greater likelihood of reported habitability problems with units."[5]

Supply

Why has housing production fallen so short of demand? There are many causes but the principal one has been the decades-long failure of the city to address the reality of the housing deficit. See Figure 8 from the LAO analysis. And Exhibit A is the failure, as the Los Angeles Times stated in an editorial, to "reform the city's broken planning and land-use system to allow more construction of housing at all price ranges."[6]

The city has not effectively updated its General Plan or community plans to recognize significant population growth since 1980. Instead of performing its core responsibility of planning for the future in a responsible and strategic fashion, the city has, for decades, ignored the growing problem and defaulted to one-offs and work-arounds.

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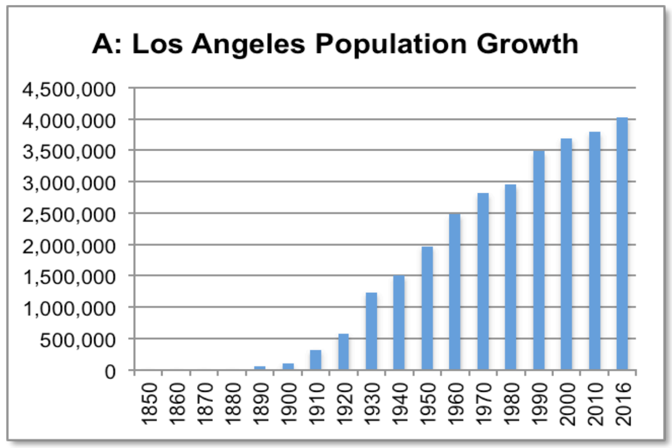
3 "Housing Element 2013-2021," *Los Angeles General Plan*, Department of City Planning, 31.
4 *The State of the Nation's Housing*, Joint Center for Housing Studies of Harvard University, Harvard Graduate School of Design and Harvard Kennedy School, 2016, 28.
5 Housing Element, Los Angeles General Plan, p. 34.
6 "Measure JJJ Could Make L.A.'s Housing Crisis Even Worse", Los Angeles Times, September 27, 2016.

As a result, the city's housing efforts have been reactive, hesitant, and ineffective, with predictable, unfortunate consequences:

- Decisions are made on a development-by-development basis, fueled by campaign contributions and public relation campaigns.
- Reactive work-arounds such as Measure JJJ—an effort that, however well intentioned, may actually slow the development of affordable housing—are promoted instead of a rational, commonsense and comprehensive plan.
- Housing efforts by city departments are poorly integrated, lack overall vision, and are not effectively coordinated with economic-development efforts.

To a large extent, the housing crisis facing Los Angeles occurred because of a top-to-bottom failure of the city to address an issue staring it in the face.

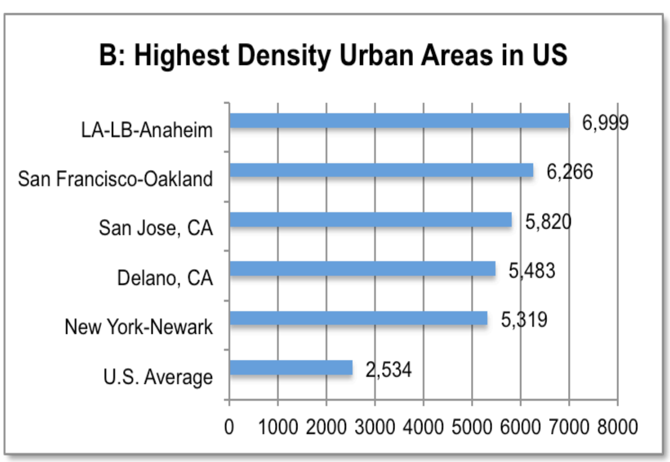
Demand



The demand for housing has grown because Los Angeles has grown. Like it or not, Los Angeles is growing and growing and growing—and national economic forces are increasingly propelling that growth.

The population in Los Angeles now tops 4 million. (See A: LA Population Growth) In recent years, the rate of increase has accelerated. According to the California Department of Finance, LA's population has grown 6.3 percent since the 2010 Census, an uptick over the more modest 2000-to-2010 increase.

That growth means the densest urban area in the U.S. is not—as many would think—the New York metropolitan area, but Los Angeles. The US Census ranks the Los Angeles-Long Beach-Anaheim corridor as the most densely populated area in the nation; in fact, it's **32 percent more dense** than the New York region and a whopping 176 percent more dense that the US average. (See B: Highest Density Urban Areas) Perceptions of Los Angeles as the sprawling, lightly populated horizontal city of 1955 tend to cloud thinking about the realities of 2017. As a 70s TV character might say: "We're dense, baby!"



What's driving the growth? All the things that have always attracted people to Los Angeles: geography, weather, glamour. But it's become increasingly clear that economic restructuring is playing a large part.

Economic forces are reshaping the geographic distribution of winners and losers in America's new economy—and precipitating a significant demographic realignment.

A recent study of economic performance in the 1990s, 2000s, and 2010s focused on how superperforming urban regions are generating more new businesses—and more jobs—than less densely populated areas.[7] The study found that 20 counties out of the national total of 3,144—just 0.6 percent—were responsible for half of the post recession national increase in business establishments from 2010 to 2014, and that over half of the 9.1 million jobs created in the 2010s occurred in only 73 counties (2 percent of the national total).

Here is a table (Table 1) of the top ten of the 20 counties that generated half of the new business establishments in the nation. Los Angeles topped the charts.

Table 1

Rank	Metro Area	Increase in Firms
1	Los Angeles	14,540
2	Miami-Dade, FL	6,790
3	Brooklyn, NY	6,510
4	Houston, TX	5,990
5	Orange County	4,430
6	Queens, NY	4,210
7	San Diego County	4,160
8	Travis (Austin), TX	3,790
9	Palm Beach, FL	3,610
10	Broward, FL	3,610

Here is a table (Table 2) of the top ten metropolitan areas ranked by increase in employment. Who is No. 1? Los Angeles.

Table 2

Rank	Metro Area	Increase in Employment
1	Los Angeles	352,840
2	Houston, TX	257,940
3	New York City	220,200
4	Cook County (Chicago)	165,680
5	Orange County	148,840
6	Dallas	130,240
7	Miami-Dade, FL	117,750
8	Santa Clara County	116,050
9	Maricopa County, AZ	115,960
10	San Diego County	101,260

These figures reveal a dramatic change from prior post-recession recoveries in the 1990s and 2000s when job and firm growth were more evenly distributed among more and less densely populated regions. Major metro areas now play the central role in firm and employment growth. These numbers "directly challenge the conventional wisdom that growth in larger and highly developed cities are by nature slower than growth rates in smaller and less developed ones."[8] The reason for the change is economic restructuring—the shift from the Industrial Economy to the Knowledge Economy.

[7] *The New Map of Economic Growth and Recovery,* Economic Innovation Group, May 2016.
[8] Ibid., p. 23.

This transition to the Knowledge Economy has been rapid – and the change is accelerating. For 60 years Fortune magazine has published a list of the 500 largest firms in America, known as the Fortune Five Hundred. Comparing the lists of 1965 and 2015 reveals how radically the national economy has transformed in fifty years.

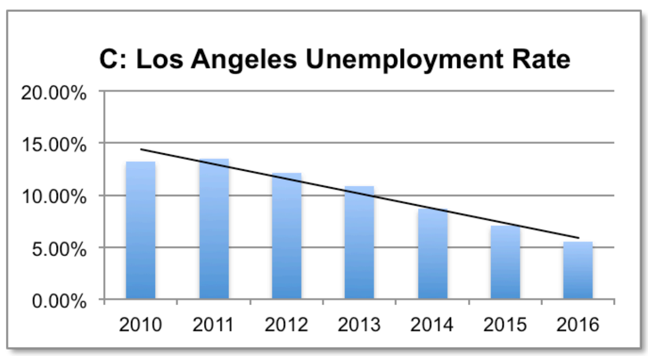
- In 1965, 74 of the top 100 firms were manufacturers. Fifty years later there were only 11 – a decline of 77 percent.
- In 1965, there wasn't a single firm from the Financial sector in the top 100; by 2015 the Financial sector represented 26 percent of the top 100 firms—the largest sector by far.
- In 1965, there wasn't a single firm from the Health Care sector in the top 100; by 2015, two Health Care firms were in the top 20.
- In 1965, not a single retailer was in the top 100; by 2015, the number one firm was a retailer and retailers were 20 percent of the top 20 firms.

Additional confirmation: Over 90% of the Fortune 500 companies from 1955 are gone. In 1958, the average age of a firm on the S&P 500 was 61 years; today, it is 18 years.

This economic transformation is causing a geographic restructuring, as knowledge- and technology-driven firms—and their jobs—are increasingly clustered in urban America. "By the 2010s, the nation's urban counties were growing faster than any other group, averaging 9.9 percent job growth—their fastest in recent history—and reinforcing the concentration of the nation's economic activity within them."[9]

Los Angeles, the densest urban region in the nation, has been the beneficiary. Firm and job growth in the Knowledge Economy has in turn sparked growth in other key industry sectors, such as leisure and hospitality, health care, transportation, and business services.

In spite of its own haphazard and often somnambulant economic development efforts, by the end of 2016 the Los Angeles economy had fully recovered from Great Recession and was effectively at full employment – which means nearly everyone who wants a job has one. (See C: Los Angeles Unemployment Rate)



Full employment means a tighter labor pool, and a tighter labor pool results in rising wages. Nationally, as the nation's job growth increased for the 75th straight month in December, wages rose 2.9 percent.[10] Economists welcome this news, but a tighter labor market and increased wages pose a dilemma in Los Angeles – because of the housing deficit.

[9] Ibid., 18.
[10] U.S. Department of Labor, January 6, 2017.

The Labor Pool Dilemma

Employers need labor, and an expanding economy creates additional demand for labor. If that demand for additional labor is not met, economic growth is impacted. An economy can't grow without enough qualified employees.

Housing plays a key role in determining the labor pool; if there is not enough housing or if housing is too expensive, the labor pool does not expand. The labor pool/growth formula is pretty simple: "Long-run growth is a function of the number of bodies in your economy. If we aren't going to build new housing to meet demand, we are going to limit economic growth."[11] A constrained labor pool will significantly constrict the future growth of the Los Angeles economy.

Historically, in-migration has helped satisfied the need to expand the Los Angeles labor pool, but the UCLA Anderson Forecast indicates that importing new employees from other states to Los Angeles becomes more difficult as the high cost of housing "discourages migration."[12]

Does a deficit in housing in a region with full employment have an impact on national and local Gross Domestic Product? The answer is yes. A University of Chicago and University of California, Berkeley study estimates the annual US economic output is **13 percent lower** due to increased constraints in housing supply in "highly productive cities such as Los Angeles."[13] That reduced economic output translates to $1.7 trillion in lost income.

Firm and employment growth in Los Angeles has created additional pressures on an already extraordinarily difficult housing market—and failure to address the housing crisis will serve as a tourniquet on future economic prosperity.

The Housing Deficit's Negative Impacts

The housing deficit has substantial social and economic costs that threaten the well being of LA residents and the future prosperity of the city. The social costs—from increasing homelessness to rising income inequality—are substantial. The economic costs are constraining the future prospects of the city and will, in turn, compound the social costs. The overall cost of the housing deficit is pervasive and expanding.

Social Costs

The housing crisis poses a substantial threat to the social fabric of the city in numerous ways:

[11] *Regional Outlook: Inland Empire*, Beacon Economics, Sept. 2016.
[12] Natalie Kitroeff, "California's Housing Shortage Will Hamper the Economy," Los Angeles Times, Sept. 28, 2016.
[13] Chang-Tai Hsieh and Enrico Moretti, "Why Do Cities Matter? Local Growth and Aggregate Growth," University of Chicago and University of California, Berkeley, Apr. 2015.

- *Increases rent burden*. Los Angeles not only has the highest share of renters in the nation but also the highest rent burden. The rent burden has historically affected the poor but is now increasingly impacting the middle class.
- *Increases income inequality*. High housing costs increase income inequality. Homeownership has been a key to household wealth creation. But homeownership in the state was only 54 percent in 2015, down 60 percent since 2005, and considerably lower than the 64 percent nationwide. That puts California 48th out of 50 states in the rate of homeownership.
- *Increases poverty*. High housing costs increase poverty rates. Adjusted for local cost of living to include housing, California's poverty rate is 23.4 percent—the highest in the nation.
- *Excessively burdens low-income residents*. "California households in the bottom quarter of income spend 67 percent of their income on housing—or four times more than households in the top quarter."[14]
- *Hurts millennials*. High housing costs have delayed the entrance of millennials to homeownership. In 2014 the median age of the first-time buyer in California was 34, three years older than the national median.
- *Forces sacrifice of basic needs*. High housing costs forces cost-burdened renters to sacrifice basic needs. Severely burdened households spend 41 percent less on food, 74 percent less on health care, and put aside less for retirement.[15]
- *Exposes additional renters to the risk of eviction*. The long-ignored issue of evictions is now identified as a principal and pervasive cause of homelessness. In a December 2016 report, the real estate firm Redfin estimated 2.7 million people faced eviction in the United States in 2015.
- *Increases homelessness*. Homelessness is a corrosive problem that saps the vitality of the city and poses threats to the lives and safety of our most vulnerable population. According to the Housing Element of the city's General Plan, "Los Angeles has the highest total number of non-sheltered homeless people in the nation."[16] More than one in five of the homeless in America live in either New York or Los Angeles, and in 2014-15, the homeless population in LA increased by 20 percent.[17]

The sequence of social costs driven by the housing deficit sequence is simple and direct:

- Insufficient Supply = More Demand
- More Demand = Increased Cost
- Increased cost + Flat Median Income = Less Ownership + More Renters
- More Renters + Insufficient Supply = Higher Rents
- Higher Rents + Flat Median Income = Higher Rent Burden
- Higher Rent Burden = Increased Evictions
- Increased Evictions = Increased Homelessness

All of these social costs—and there are others—are taking a significant toll on individuals, families, and communities in the city. Addressing major problems like

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[14] "California's High Housing Costs", 26.
[15] *The State of the Nation's Housing*, 5.
[16] "Housing Element," *General Plan,* 40.
[17] *The State of the Nation's Housing*, 32.

homelessness and increased levels of poverty means, first and foremost, addressing the housing crisis.

Economic Costs

The housing deficit in Los Angeles is having an immediate and long-term impact on economic prosperity because there is a direct link between housing and economic growth. There are four principal reasons:

- High housing costs constrict the labor pool—and an economy can't grow without enough qualified employees.
- A decline in homeownership significantly reduces household wealth formation, particularly among minority populations.
- Increasing housing costs in Los Angeles exert an enormous cost burden on homeowners and renters that dramatically reduces their consumption spending.
- High housing costs are a substantial barrier to household formation—and additional household formation is a key component of an expanding economy.

These four impacts are occurring in the midst of a significant geographic restructuring of the national economy. As stated above, substantial economic data shows that post-Great Recession economic growth is primarily occurring in large metropolitan areas—including Los Angeles. That shift—in both firm and job creation—will only increase housing demand in the city. Unless that demand is met, the labor pool will not expand, the economic recovery will stall, and future growth will be severely constrained.

Housing and Labor Supply

Housing and economic prosperity are inexorably tied because the cost of living (of which housing is a principal driver) directly impacts the economy. The ability of firms to hire workers at reasonable cost is the primary component of business-location decisions because labor is the principal cost of doing business. High housing costs raise the cost of living with two results, and both are detrimental:

- If the cost of living related to household income is too high, folks leave for other regions—and deplete the labor pool.
- If a higher cost of living increases wages and makes labor costs too high, firms leave.

Los Angeles has recovered from the Great Recession; but what's the prospect for future economic growth? The finance firm Kiplinger ranked the top ten states (Table 3) in 2016 employment growth based on rate of growth – with California coming in as No. 10.

Table 3

	State	Job Growth	Jobs	Unemployment
1	Idaho	3.5%	23,580	3.8%
2	Arizona	3.2%	84,380	5.5%
3	Utah	3.1%	42,720	3.1%
4	Oregon	3.0%	53,360	5.6%
5	Florida	3.0%	242,870	4.9%
6	Georgia	3.0%	128,030	5.5%
7	Washington	2.8%	88,320	5.7%

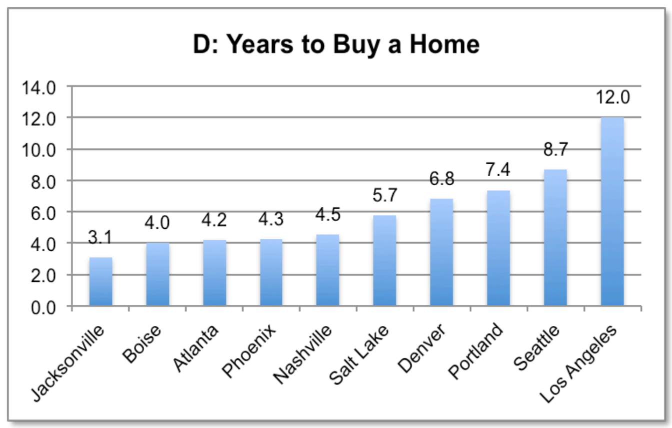
8	Tennessee	2.8%	80,980	5.1%
9	Colorado	2.8%	68,630	3.2%
10	California	2.7%	433,400	5.6%

Now let's compare median home price and the household income for the principal city in each of those states (Table 4). Los Angeles has nearly the highest home value, just a bit less expensive than Seattle, but its median household income is far less:

Table 4

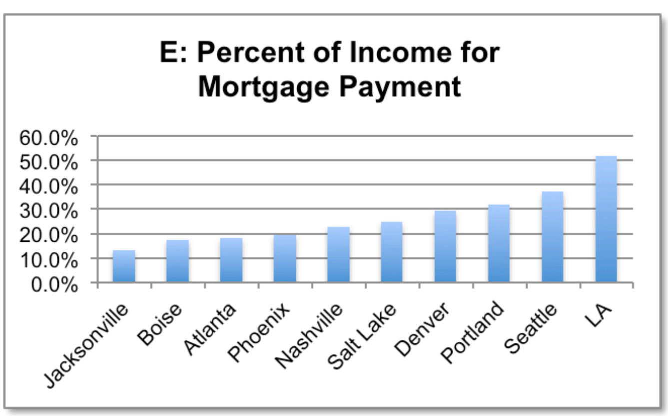
	City	Home Value	Median Income
1	Jacksonville	$144,300	$46,764
2	Atlanta	$199,700	$47,527
3	Phoenix	$202,300	$47,326
4	Boise	$203,300	$50,323
5	Nashville	$215,300	$47,621
6	Salt Lake	$271,400	$47,243
7	Denver	$366,500	$53,637
8	Portland	$405,700	$55,003
9	Los Angeles	$603,900	$50,205
10	Seattle	$612,400	$70,594

Now let's compare median home price and household income for the principal city in each of those states and chart the impact of trying to buy that median-priced home with that median household income. Or: how many years of that median income would it take to buy a home? (See D: Years to Buy a Home)

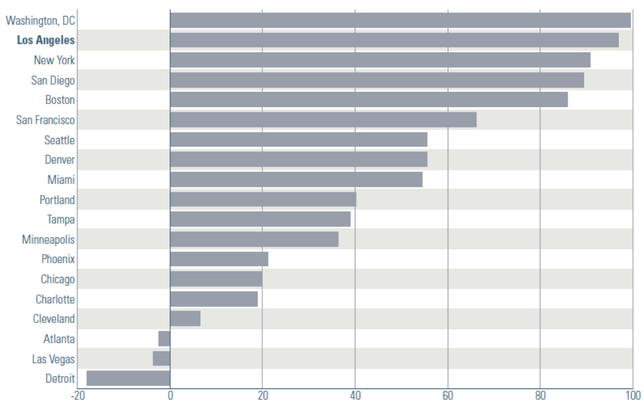


It would take a resident of Los Angeles **12 years** earning the median household income of $50,205 (and using every penny of that income) to buy a home in LA – significantly higher than in these cities.

Just to drive home the point, we can look at it another way: What percentage of household income would it take to buy that median priced home in each city? (We'll figure 25 percent down and a fixed 30-year mortgage at 4 percent). Our unhappy Los Angeles household would use over half of their household income (a whopping 51.7 percent) for mortgage payments (See E: Percentage of Income for Mortgage Payment). In this scenario, our LA resident would pay 109 percent more of their household income than Salt Lake City homeowners. That's a hefty price to pay for the joys of homeownership.



Variance in Metropolitan House Prices, 1998-2012



Source: Federal Reserve Bank of St. Louis. *The Boom and Bust of U.S. Housing Prices from Various Geographic Perspectives* Federal Reserve Bank of St. Louis Review, September/October 2012.

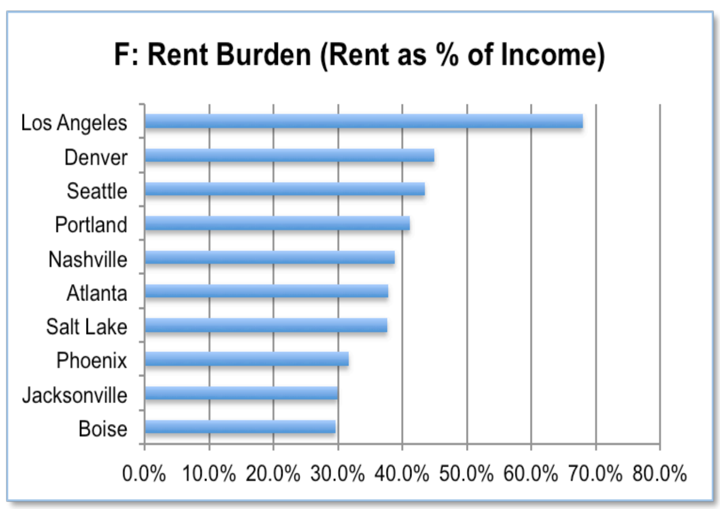
What's causing this crunch in LA? The rise in home prices and a relative flat level of median income. Here's a chart from the Federal Reserve Bank of St. Louis of the change (variance) in house prices from 1998 to 2012 (Chart Titled: "Variance in Metropolitan House Prices, 1998-2012)

And as noted in the city's Housing Element of the General Plan, LA's median income has lost ground. "It is important to note that, since 2000, the City's median income has moved further below that of the County, the State and the country. In 1990, the city's income was nearly the same as the country as a whole."[18] According to the 2014 UCLA study *Impacts of the Widening Divide*, "Los Angeles housing prices have grown about four times faster than incomes since 2000."[19] This sandwich squeeze—flat median income and rising housing prices—explains the falling rates of homeownership.

Increased Cost Burden on Renters

Of course, it's not just home ownership that has become unaffordable; housing in LA is increasingly unaffordable **at every income level.** The most pain has been borne by renters, and LA is the metropolitan area with the highest share of renters in the nation.

Rent burden is the term used to describe the ratio of rent to income. Los Angeles "consistently exceeds the nation in both the share of renters burdened and the severity of the burden."[20] Nationwide, the number of cost-burdened renters rose by 3.6 million from 2008 to 2014, and the impact has spread from low- to moderate-income households, "especially in higher-cost coastal markets" such as Los Angeles.[21] That expansion of substantial rent-burden means, "50 percent of mid-range renters in Los Angeles experience some sort of burden."[22]



Los Angeles's rent-burden problem is particularly pronounced because the city has a relatively low median household income (lower than the county or state median) and very high median rental rates—quite similar to those of New York, for example. Chart F compares the rent burden (rent as a percentage of income)

[18] "Housing Element," *General Plan,* 8.
[19] Ray, *Impacts of the Widening Divide*, 3.
[20] Ibid., 1.
[21] *The State of the Nation's Housing ,* 4.
[22] Ray, *Impacts of the Widening Divide,* 11.

for Los Angeles and those nine cities we've compared above. We're using the Zillow Rent Index number for each city. If we compared the rent burden with other California cities, the difference would not be as dramatic, because housing costs are so much higher in our state. But Los Angeles "consistently exceeds the nation in both the share of renters burdened and the severity of the burden."[23]

The high cost of housing in Los Angeles—for renters and homeowners—is a simple supply-and-demand problem. The Legislative Analyst Office's report *California's High Housing Costs* sums up the problem succinctly: "Between1980 and 2010, the number of new units in the typical U.S. metropolitan area grew by 54 percent—but only by 20 percent in Los Angeles."[24] The city's own Housing Plan is more specific; it cites the "historical deficit of housing growth compared to population. Overall, the rate of population growth has exceeded housing growth by 42 percent from 1980 to 2010."[25]

Economic Impact of Home Ownership

Homeownership has been a wealth-creation vehicle for the nation's middle class, but homeownership rates have fallen significantly; the rate in California is down 60 percent in ten years.[26] That decline impacts wealth creation and consumption spending. The growing disparity of wealth in America is greatly impacted by homeownership, and the door is closing on homeownership for middle- and lower-income residents. A report by the Joint Center for Housing Studies of Harvard University offers these startling statistics on household wealth at the national level:[27]

> *Households with low homeownership rates face enormous disadvantage. The median net household wealth of blacks ($11,000) and Hispanics ($13,700) is roughly one-tenth that of whites ($134,200).*

The higher costs of home ownership have really impacted millennials. The age of first-time homebuyer in Los Angeles has risen to 34, which is three years older than the national median.[28]

Household Formation

New household formation is a cornerstone of economic growth. Household formation boosts housing demand and construction—and the consumption of everything in that new house. But household formation has lagged during the recovery from the Great Recession, and that has also led to a less-than-robust housing recovery. A UC Berkeley analysis stated, "We're not seeing a recovery in the type of household formation that is most directly affected by the economic cycle—within-age-group headship rates—despite the notable improvement in the job market in recent years."[29]

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[23] Ibid., 1.
[24] Alamo, *California's High Housing Costs,*11.
[25] "Housing Element," *General Plan,* 34.
[26] *California Outlook*, Beacon Economics, Oct. 2016.
[27] *State of the Nation's Housing*,15.
[28] Alamo, *California's High Housing Costs*, 29.
[29] Jed Kolko, "Who Is Actually Forming New Households?" Terner Center for Housing Innovation, UC Berkeley, August 17, 2015

Economists are digging into the data to figure out why, and the consensus is the decline was driven by millennials. Why? "Most young adults are living with their parents."[30] Economists point to a number of reasons for this, including slow wage and job growth: "Employment recovery hasn't gotten young adults out of their parents' basements yet."[31] Another reason may be that millennials have been less likely to marry or cohabitate with a partner because couples (perhaps understandably!) are far less likely to choose to live with their parents. Student-loan debt may also play a role: post recovery, there's been no decline in the percentage of 25-29-year-olds living with their parents, "and some studies suggest that the cause is the rise of student loan debt."[32]

What's been the impact on household formation by millennials in Los Angeles? "There was an 8 percent decline in the numbers of households headed by individuals under 34 years old since 2000. There was a troubling 29 percent decline in the number of homeowners under the age of 34 since 2000."[33]

We can safely attribute a large portion of the decline of millennial household formation and homeownership to the high cost of housing. As the economy and wages grow, there will be a pent-up demand from millennials for housing. The issue is whether Los Angeles will capture that growth—or whether less-expensive housing in other locales will prove enticing. Recent migration studies show that lower-income folks are leaving Los Angeles while higher-income earners are moving in. Millennials—a group that every region in the nation is courting for economic development—may not have the income to remain in LA and may take their education, talent, and economic impact elsewhere.

What Other Cities Are Doing

Los Angeles is not the only city facing a housing crisis. American cities are using a variety of tools to create more below-market-rate housing because developers have not built enough units to meet the demand. It's the "below-market-rate" modifier that's the rub.

Developers and homebuilders are in the housing business to make a profit, and to maximize the profit they make. Developers require a certain rate of return, and the highest rate of return is in high-end development; the lowest is in affordable units. It is the same calculus we see in the automotive industry: manufacturers prefer to make large SUVs that get poor gas mileage rather than smaller, more-energy-efficient cars **because that's where the profits are.**

But just building high-end housing obviously won't solve the affordable housing deficit, much less the homeless issue. The housing demand in Los Angeles is broad based; the market wants a diversified portfolio of housing—but the higher profits in the high-end market work against producing an adequate amount of middle-income and affordable housing.

Even if Los Angeles were to remove all the roadblocks and speed bumps to housing

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[30] Fred Furlong, "Household Formation among Young Adults," Federal Reserve Bank of San Francisco, May 19, 2016.
[31] Kolko, "Who Is Actually Forming New Households?".
[32] Furlong, "Household Formation," 2.
[33] "Housing Element," *General Plan,* 11.

development, investment in housing would still flow to projects generating higher rates of return. That is why cities have intervened with a combination of requirements and/or incentives to encourage production in below-market-rate housing.

An increasing number of cities are using zoning as a wedge to encourage new workforce housing. And the most widely used tool is Inclusionary Zoning (IZ), which requires (or encourages) developers to include below-market-rate rental or for-sale housing as part of development projects. More than 500 cities and counties in 27 states and the District of Columbia have adopted an IZ policy.[34]

IZ can be mandatory (*x* percent of units must be below market-rate) or voluntary (we hope x percent of units will be below market-rate) or some combination of mandatory and voluntary. Mandatory IZ has specific requirements, such as:

- Eligibility (based on a certain percentage of median income)
- Term (length of time the affordability requirement is in place)
- Opt-outs (in lieu of payments, commitment to build off-site units)

IZ offers incentives to offset the cost of including affordable units in the development and equalize the rate of return. What kind of incentives?

- Expedited review and approvals
- Direct subsidies
- Density bonuses
- Tax and fee abatements/waivers
- Relaxed requirements, such as reduced parking

Cities mix and match requirements and incentives in horse-trading with developers, with each side attempting to extract the most favorable resolution. Some particulars are more valuable to a jurisdiction and some to a developer. Examples include:

- Expedited fast track review = low fiscal impact on city, high fiscal impact for the developer
- Waiving development fees = high fiscal impact on city, medium impact on developer

What's the best way to achieve the desired level of a diversified portfolio of housing? The answer is some combination of incentives and requirements that's adjusted for the kind of housing (for example, workforce, market-rate, homeless). Currently, development deals in LA are struck after myriad negotiations with numerous players (for example, council districts, city staff, neighborhood groups). The results have not reduced the housing shortfall.

Deploying a more systematic approach that takes into account and effectively values incentives and requirements would make the process more rational and predictable. Markets hate unpredictability, and so moving to a more predictable process would improve the market. One way to encourage a more rational process would be to turn to the incentive/disincentive professionals: trained economists. Economists disagree on

[34] Stockton Williams, Ian Carlton, Lorelei Juntunen, Emily Picha, and Mike Wilkerson, *The Economics of Inclusionary Development,* Urban Land Institute, 2016.

many things, but they understand and can monetize incentives/disincentives as a marketplace mechanism. Tapping into the expertise of local universities and their economists to develop a reasonable package of incentives/disincentives that stimulates housing production at reasonable costs could help the process significantly.

Coming to Grips with Housing

The failure of Los Angeles to come to grips with the housing issue is a classic example of the You Can't See the Forest for the Trees aphorism. Instead of recognizing the direct relationship between housing and economic growth, political and civic leaders in Los Angeles have focused their attention on other less crucial issues—or only considered a piece of the housing dilemma, such as housing for the homeless.

A sample of this attitude can be found in the well intentioned but largely ignored Los Angeles 2020 Commission report. The report tended towards a gloom and doom portrait of Los Angeles to encourage some urgency among elected officials. Some of its observations:

- "Los Angeles is barely treading water, while the rest of the world is moving forward."
- "We risk falling further behind in adapting to the realities of the 21st century and becoming a city in decline."

The report cited some key factors driving this decline, including "dramatic budget shortfalls", "traffic and congestion" and "public education fall[ing] short of the mark". To meet these challenges, the report offered a series of recommendations, from moving the date of municipal elections to establishing a regional tourism authority.

And housing? It's an issue that didn't even rate a place on the recommendation list. The closest the report comes to housing is its last recommendation to update community plans—but the reasons it gave to do so include: "Transit, public safety, education, recreation, workspace—these most central aspects of a thriving community rely on comprehensive, up-to-date community plans." But not housing.

The Solution

For Los Angeles to solve its housing crisis, it first needs to create the right framework for understanding the problem. This includes:

- Recognizing that solving the housing crisis is the single most important economic development issue facing the city.
- Acknowledging that the issue cannot be solved by a business-as-usual attitude that has already failed.
- Abandoning efforts to solve this crisis with workarounds and public relations projects.
- Understanding that the housing crisis requires harnessing private sector capacity and capital to meet the need. Sources of public sector capital—federal, state, and local funding—are so limited that they can only supplement the private sector, not be the prime driver of housing development.

- Developing and executing a reasonable and rational strategic implementation plan with attainable goals and clear metrics to close the housing gap.

Let's be direct. The answer to the housing crisis is simple: increase supply by building many more housing units. The conditions are right:

- There is enormous market demand, which will only increase as millennials create new households.
- There is enormous availability of capital to finance new housing.

The issue is changing the mindset and process. Solving the housing crisis requires neighborhoods, communities, and political and civic leaders to recognize that Los Angeles in 2035 will be different from the Los Angeles of 1965. It is far better to strategically shape the future than allow the future to be imposed upon us. Shaping that future means assessing where LA is now—and where we want LA to be. That means asking hard questions—and questioning conventional wisdom. Here are just a few of those questions:

- *Are the current levels of impact fees appropriate?* For example, what's the appropriate school impact fee when the Los Angeles Unified School District has declining enrollment?
- *Are parking requirements correct?* In an era of expanding mass transit, Uber, Lyft, and soon-to-arrive self-driving cars, what's the right mix of parking?
- *Do current zoning designations make sense?* Could the highest and best use of currently zoned industrial land—in an era of manufacturing consolidation—be residential? Rezoning some industrial land could reclaim land for workforce and affordable housing without impacting existing single-family neighborhoods.

The housing crisis requires a commitment to reconsider long-held perceptions. *We've always done it this way* is a phrase better suited as a tombstone epitaph than as the city's standard operating procedure.

Every mission needs goals:

- Create a portfolio of housing that responds to the needs of all Angelenos. That means market-rate housing, affordable housing, workforce housing, housing for the homeless, transit-oriented housing—housing in all categories.
- Set a target to permit and build X-number of new housing units over the next ten years to meet market demands. What's the magic number? Demographers, economists and housing experts can debate the issue, but the right number is the number that brings the cost of housing in line with a reasonable percentage of household income.
- Upgrade, rehab and preserve existing housing units over the next fifteen years to ensure affordable older units aren't lost even as new ones are built.

Guidelines

Los Angeles desperately needs an effective, strategic housing plan. Such a plan should be grounded in some common sense guidelines, such as:

- Make the housing development process reasonable, rational and predictable.
- Remove special interest money from housing development decisions.
- Restructure city departments involved in housing and economic development to better coordinate efforts.
- Update the General Plan and Community Plans by a date certain—and then keep them updated.
- Use the knowledge and experience of developers, planners and community members to review the City's fee structure with a goal of reducing the cost of building homes.
- Review and update incentive programs to develop workforce housing.
- Work with other cities to streamlines state regulations.
- Encourage innovation, new ideas and new technologies.
- Ensure the private and nonprofit sectors are full partners in the housing effort.
- Secure investment in housing from major city, county and state pension funds.
- Leverage the intellectual expertise of area colleges and universities to develop housing strategies that are reasonable, achievable and make economic sense.