Sacramento Housing & Redevelopment Agency

# REPORT TO COUNCIL AND REDEVELOPMENT AGENCY
## City of Sacramento

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**STAFF REPORT**
**May 29, 2007**

**Honorable Mayor and Members of the City Council**
**Honorable Chair and Members of the Board**

**Title:** Downtown Housing Strategy

**Location/Council District**: Downtown, Districts 1, 3, and 4

**Recommendation:** This workshop item will review the current downtown housing market and the Agency's investments to support housing development over the past five years. Staff will also seek direction on proposed strategies for continued housing investment to support a successful downtown.

**Contact:** Lisa Bates, Community Development Director, Sacramento Housing and Redevelopment Agency (SHRA), (916) 440-1316; Leslie Fritzsche, Downtown Division Manager, City of Sacramento, (916) 808-5450

**Presenters:** Lisa Bates, Community Development Director, SHRA, and Leslie Fritzsche, Downtown Division Manager, City of Sacramento

**Department:** Sacramento Housing and Redevelopment Agency and Downtown Development Department

**Description/Analysis**

**Issue:** Since 1990 1,773 homes have been developed in the downtown, most of which were in developments requiring Agency assistance. The downtown is realizing a stronger market, but external market conditions and fluctuations affect the viability of privately developed housing. Using a study from the Brookings Institution that examined successful downtowns throughout the nation, staff will review Sacramento's downtown against the study's markers for success.

Using the markers as a base, staff will present recommended strategies to foster a healthy downtown that includes housing for all income levels. These strategies build on past Council and Agency direction to focus downtown housing resources in the Central City, promote the development of affordable, mixed income, and market rate housing and build upon the strength of the downtown neighborhoods.

**Committee/Commission Action:** None. Staff presented this report to the Downtown Sacramento Partnership Executive Committee and to the SHRA Commission on May 16, 2007. In addition, staff has notified the Planning Commission members of this workshop.

**Policy Considerations:** The City Council and Agency have been exploring a number of housing policies through the General Plan and the City's Economic Development Strategy processes. This workshop provides an update on the downtown housing market and proposes strategies for how the Council and Agency might direct investment to ensure that downtown becomes a "vibrant and healthy place to live and work."

**Environmental Considerations:** Not a project as defined by the California Environmental Quality Act (CEQA)[CEQA Section 21065 and CEQA Guidelines Section 15378 (b)(4)].

**Rationale for Recommendation:** The City Council has been exploring a variety of housing related issues through a series of workshops, including the General Plan process and Economic Development Strategy. The Downtown Housing Strategy workshop builds on many of the principles included in the series of workshops and is a complementary piece of an overall housing strategy for the City. Through these workshops there has been an increasing awareness of the linkage between economic development and housing development, emphasizing the need to provide housing for a range of income levels and household types. The proposed Downtown Housing Strategy seeks to foster the success of market-driven development while maintaining housing options for households at all income levels.

**Financial Considerations:** Strategies are suggested for existing Merged Downtown tax increment funds. However, new programs, specific projects or funding allocations under the strategies will be brought to the City Council for approval.

**M/WBE Considerations:** The items discussed in this report have no M/WBE impact; therefore, M/WBE considerations do not apply.

Respectfully Submitted by: _____
ANNE M. MOORE
Executive Director, SHRA

_____
LESLIE FRITZSCHE
Downtown Division Manager, City of Sacramento

Recommendation Approved:

_____
for RAY KERRIDGE
City Manager

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**Attachment 1**

## WHO LIVES IN DOWNTOWN SACRAMENTO? CONSIDERATIONS FOR A HOUSING INVESTMENT STRATEGY

Throughout 2005 and 2006, the Metropolitan Policy Program of the Brookings Institution published numerous studies on the challenges facing metropolitan America and proposed strategies for sustainable growth. One study in particular, "Who Lives Downtown?" analyzed demographic, market, and social trends in 44 downtowns throughout America – unfortunately, not Sacramento – and used these trends to establish typologies ranging from fully developed, successful downtowns to those that are declining.

Staff from the Sacramento Housing and Redevelopment Agency (SHRA) applied Brookings research to downtown Sacramento, primarily using housing market, demographic and income data produced by the Gregory Group. The Brookings' study identified the markers listed below for successful downtowns, urging urban leaders to understand these patterns and use them to guide their investment decisions:

- A marked resurgence of population growth in the 1990s, shifting significantly to singles and unrelated individuals living together;
- A high percentage of younger adults (ages 25 to 34), the "hip downtowners;"
- Increasing household incomes;
- Ethnic diversity;
- Higher density housing;
- Critical mass of housing and jobs;
- Growth in homeownership; and
- Increased housing values.

The study also recognized that downtowns are increasingly home to some of the most affluent and poorest households, a concern raised in another Brookings Institution report, "Where Did They Go? The Decline of Middle-Income Neighborhoods in Metropolitan America." Staff addresses all of the markers, plus this social equity concern in recommending its housing investment strategy for the Downtown. In this report, and in the accompanying power point presentation, "downtown" is used synonymously with "central city." For this discussion, this includes the area bounded by Highway 50 to the south, Highway 80 to the east, Interstate 5 to the west and the railroad tracks to the north.

### Who Lives Downtown? The Demographics

Downtown's household population grew an impressive 8.7 percent from 2000 to 2006, compared to 8.2 percent citywide. (Brookings projected that successful downtowns should sustain a one percent annual growth rate over 30 years, recognizing fluctuations between decades. Downtown's 1.5 percent average annual growth rate since 2000 fits

comfortably within this 30-year goal.) In 2006, downtown's households represented 11 percent of the City's household population, the same percentage as in 2000.

When total population is considered, as opposed to household population, downtown percentages drop due to the high percentage of single-person households downtown. For example, from 2000 to 2005, the City's total population jumped 10 percent (showing the effect of North Natomas and South Sacramento growth spurts), while the downtown, overcoming a decline during most of the 1990s, picked up speed after 2000 to achieve a five percent increase by 2005.

Downtown's population picture is captured most dramatically in the number of younger people aged 25 to 34 years living in the central city, 26 percent compared to 17 percent citywide. Brookings' marker was 25 percent for this age group, considered by many researchers to be the entrepreneurial and technologically-savvy class that creates jobs for local and global consumption. However, it should be noted that downtown has also shown an impressive increase in older workers, particularly from 1990 to 2000. At the other end of the age spectrum, the younger age group from 15 to 24 years declined significantly from 15 percent of the downtown's population in 2000 to ten percent in 2006.

Single persons and unrelated individuals living together dominate the downtown scene at 77 percent of all households in 2006, nearly double the proportion of singles citywide. Married couples with children (4.7 percent) and single parents with children make up ten percent of the downtown population -- exactly the percentages the Brookings' study found in its survey of 44 downtowns.

The predominance of single persons and other households without children are the major source of demand for new housing units in downtowns across the country.

Racial and ethnic diversity downtown shows a fairly even split between white and minority populations in 2006. The white population has been steady at 54 percent, with growing populations of Hispanics and persons of two or more races. The African-American population is declining, and Asian households are declining at a very slow rate.

Many commentators on urban trends view diversity and tolerance in America's downtowns as important factors in attracting 25 to 34 year olds and the creative class of individuals that propels economic growth.

Downtown median household income increased 11 percent from 2000 to 2006, but could not keep pace with the 19 percent increase in the City as a whole. Although downtown proportionately has more lower income residents than the City, a number of its census tracts were changing demographically as higher income residents moved in and housing values increased.

Income Disparity and Loss of Workforce Housing. One of the Brookings' descriptors for thriving downtowns was growing income disparity, leaving downtowns housing the

affluent and the poor. A result of rising economic inequality and the associated decline of the middle class "hollows out" middle class neighborhoods, leaving them either predominately poor or affluent. The Brookings Institution's recent study, "Where Did They Go? The Decline of Middle Income Neighborhoods in Metropolitan America," included data on the Sacramento Primary Metropolitan Statistical Area. SHRA staff applied their research methodology to the downtown and City, based on 2000 census tract data. While certain income trends present challenges, the "hollowing out" of middle class neighborhoods has not yet arrived.

For example, the northeast quadrant of the central city saw dramatic increases in median incomes ranging from 70 to 86 percent. These midtown neighborhoods generally north and east of the central business district[1] include traditional single family homes and smaller rental properties. However, on the other end of the income spectrum, the two poorest census tracts[2], located in the central business district, exhibited the least change. Overall, from 1990 to 2000 the median household income in downtown neighborhoods gained slightly on the City, climbing from 60 to 64 percent of the City's median household income, but remains disproportionately lower.

The Brookings study considered fully developed downtowns to have approximately half of their census tracts similar in income to that of their respective Metropolitan Statistical Areas (MSAs), which in the Sacramento region is higher than the City's median income. Given that difference, downtown does not approach the benchmark since only 21 percent of downtown census tracts approximate the City's median household income.

As home prices increase and more affluent residents move into downtown, as they have since 2000, additional neighborhoods will be entering the category of "middle class." As a result, the loss of housing for the lower income workforce is one of the challenges presented by downtown's increasing affluence.

Density matters

New developments proposed for downtown will alter the City's skyline. Given the diminished inventory and size of vacant lots, the proposed homeownership and rental developments plan higher density residential living that will increase the downtown's density significantly from its estimated 34 dwelling units per acre in 1990.

Downtown's density exceeds Brookings' first benchmark for fully developed, successful downtowns: having at least 23 dwelling units per acre. The City should be able to meet the second benchmark - having sustained housing unit increases for two or three decades –in the future if current development trends continue. The Brookings study considers density to be vital to the downtown values of walkability and accessibility to

[1] Census tracts 4, 11, and 14 primarily include the following neighborhoods: Boulevard Park, New Era Park, Marshall School, Winn Park, Capital Avenue, and the southern portion of Mansion Flats.
[2] Census tracts 7 and 10, which are generally bound by the river on the west, H Street on the north, 12th Street on the east and Capital Avenue on the south.

jobs; it is also necessary to support amenities, facilities, transit and services that determine downtown character.

Sacramento's recent update of its Urban Design Plan for downtown explores all the facets of density and its integration with surrounding development. It is an important part of the City's development strategy for a successful downtown.

Critical Mass of Amenities and Jobs: The "Virtuous Circle"

Stable employment, amenities, and residents are linked to one another in the creation of successful downtowns. Employment attracts residents who will move downtown if the right product exists and if a wide range of cultural, recreational and "consumption" amenities are present. They, in turn, create the demand for more amenities and produce additional employment.

The Brookings' study contends that this critical mass does not occur by accident. A city's development climate, investment in amenities, and housing strategy geared to younger residents and homeownership are important elements of success.

Homeownership Downtown

Homeownership rates downtown have remained stagnant at 12 percent since 1990. This rate is half of what the Brookings research considers important for fully developed, successful downtowns. Equally significant is whether the rate is growing, as it did by 36 percent from 1990 to 2000 in the downtowns it studied. The following cities achieved these homeownership rates in 2000: Chicago - 41 percent; Denver - 36 percent; Austin - 35 percent; and Indianapolis - 27 percent.

However, downtown is on the verge of a breakthrough in homeownership. In the next five years, the homeownership rate will increase to new highs if the following developments are built and sold:

- 13 percent if housing under construction is built and sold;
- 19 percent if housing under construction plus approved projects are built and sold; and
- 28 percent if all the above housing, plus proposed developments are built and sold.

The number of new homeownership developments planned for downtown (estimated at 5,500) primarily in condominiums, is a remarkable departure from the past. Brookings and other urban policy analysts view downtown homeownership as creating stability and reinvestment.

The planned homeownership product and pricing reflects the types of housing demanded by an upper-income market who in the past commented that the "right product" did not exist downtown: (The projected pricing listed below is taken from a sample of the new developments.)

| | |
|---|---|
| Townhouses: | $400,000 - $800,000 |
| Lofts: | $300,000 - $1,000,000 |
| Mid-rise condominiums | $320,000 – $450,000 |
| High-rise condominiums | $300,000 - $1,000,000 |
| Existing homes: | $450,000 and rising |

Modest income households (earning approximately $45,000 to $70,000) could afford a home ranging from $200,000 to $250,000. [3]

Increased Housing Values

Homeownership. The value of central city homes as measured in median resale prices increased 250 percent over the last ten years (1995 – 2005), compared to a 192 percent increase in the City. The downtown single family housing price averaged $483,170 in 2006 and was higher than currently selling new homes in surrounding cities and the unincorporated county. Twenty-five percent of downtown's single family homes sold for over a half-million dollars.

Over the last nine months, existing condominiums downtown sold for an average of $341,813. This resale price was similar to the new condominium prices in surrounding cities and the unincorporated county.

Increased housing values correlate with the increasing affluence of downtown residents. It has reversed the disinvestment in downtown neighborhoods so prevalent in the 1970s and 1980s. Higher housing values also generated investment in new infill development downtown as a new market for urban living materialized.

Apartments. Downtown's average $1,100 monthly rent in 2006 was slightly higher than rents citywide. Apartments averaging these rents would be affordable to households earning approximately $35,000, if they were paying 30 percent of their income for rent.

Rents in the six newest apartment developments downtown averaged $1,699 (ranging from $925 to $4,000 for penthouses), reflecting market demand for new, modern units with such on-site amenities as spas, concierge services, business and fitness centers, and ground floor retail. Low vacancy rates downtown, as reported by Arroyo and Coates' Sacramento Region Quarterly Market Report, similarly reflect the overall demand for downtown living.

"Affordability insurance." A portion of downtown renters have been protected against significant rent increases by living in publicly assisted housing. Of the 1,773 privately owned units financed in downtown since 1990, 60 percent had affordability restrictions limiting rent increases. In addition, 93 percent of the total units developed were in developments that had public assistance. The Sacramento Housing Authority also houses 656 seniors and 293 families downtown.

[3] The calculation of affordable home prices is based on current interest rates for 30-year fixed-rate mortgages, a five percent down payment, taxes, and insurance (mortgage, property and flood).

In addition, recent citywide commitments will benefit the poorest residents downtown:

- $15 million in downtown tax increment funds for residential hotel replacement, rehabilitation and new construction (citywide);
- Ten-Year Plan to End Homelessness, establishing the "Housing First" collaborative with county agencies to move homeless persons into housing;
- Preservation of HUD-assisted developments, such as Washington Square Apartments in Alkali Flat; and
- Historic preservation/conversion of Globe Mills as affordable senior housing.

**Summary of "Who Lives Downtown?" Are We Hitting the Benchmarks?**

- Demographics on target:
  - singles dominate
  - younger (ages 25 to 34) persons prevail, followed by older and retired workers
  - diversity strong and stable
  - incomes rising, raising concern for workforce population
- Higher density housing already here and increasing
- Critical mass of jobs and amenities evident through city and private investment
- Homeownership on the increase with new development, but prices beyond modest income affordability
- Increased value of housing significant

**Recommendations for a Housing Investment Strategy for Downtown**

The demographic, housing market, and income trends described above help tailor development and investment strategies for the downtown. Three challenges emerge from the application of the Brookings Institution's study that can become the framework for a Housing Investment Strategy:

1. Improve the conditions for success of market rate housing.
2. Invest housing funds in mixed-income apartments.
3. Maintain or increase the commitment to Single Room Occupancy (SRO) preservation and replacement.
4. Provide homeownership opportunities to modest-income households.

<u>Investment Strategy 1: Improve the conditions for success of market rate housing</u>

For many years, the City of Sacramento has understood Brookings' exhortation that successful downtowns do not occur by accident. It has laid the groundwork for private investment downtown through major activities that need to be maintained or increased:

- Public funding of significant amenities, including cultural facilities and events, the docks and riverfront, parks, tree canopies, historic street lights, traffic calming, sidewalk café ordinances, etc.

- Improved development climate through increasing the predictability in permitting and processing of building applications and adopting exceptional planning and design guidelines.
- Strategic public investments in infrastructure, including Light Rail and Amtrak transit hub, water and sewer line replacements, and flood control.
- Attention to economic growth, targeting education for tomorrow's workforce and the "knowledge industry" to retain talent and be competitive in the global market.

These activities create the conditions under which market rate housing can succeed.

Investment Strategy 2: Invest housing funds in mixed income apartments.

Investing in workforce housing will create affordable mixed-income developments for households earning from $20,000 to $40,000 a year. A critical element is the proactive role played by SHRA and City planning and development in site selection, development approval, and partnering with affordable housing developers.

- Develop publicly owned lands to create the feasibility for affordable units. Leverage the same resources from CADA and PERS as they similarly provide new residential units along the R Street Corridor and throughout CADA's jurisdiction.

- Use the City's affordable housing funds for gap financing of downtown developments. This would include approximately half of the downtown redevelopment bond proceeds ($22 million) allocated to housing.

- Support state applications for tax credits, private activity bonds, and the housing programs of the State Department of Housing and Community Development

- Fund off-sites with non-housing funds (described above)

Investment Strategy 3: Maintain or increase commitments to SRO preservation and replacement.

In 2006 the Redevelopment Agency and City Council committed funding and adopted policy to preserve downtown housing for very-low and extremely-low income residents. In March the Redevelopment Agency committed $15 million in Downtown housing funds to preserve existing residential hotels and to build new efficiency apartments. In September the City Council amended the Residential Hotel Ordinance to add additional relocation benefits for tenants displaced by closure of an existing downtown residential hotel. In addition, the Council adopted goals of preserving a minimum of 712 single-room occupancy units in downtown and rebuilding the total inventory to 1000 units citywide.

The City's commitment to preserving and rebuilding the inventory of single-room occupancy and efficiency apartment units has been marketed to the development community through a Request for Applications. One application has been received and

staff is aware of at least one other application in preparation. The sum of these two funding requests is expected to be approximately $7 million and will result in development or preservation of approximately 130 units.

Investment Strategy 4: Return homeownership opportunities to modest-income households (those earning from $45,000 to $70,000, with an ability to purchase homes ranging from $200,000 to $250,000)

This strategy may present the greatest challenge because most housing funds available to local governments do not allow their use for households earning more than 80 percent of the area median income (approximately $43,000 for a two-person household). Redevelopment's tax increment funds do allow expenditures for households at 110 percent of the area median income (approximately $59,000 for a two person household), but the layers of restrictions make it almost impossible to fund homeownership at those income levels. However, a homeownership incentive program can be developed to include some or all of the following features:

- Provide direct assistance to homebuyers with deferred second loans through the State of California's BEGIN program, funded in November 2006 through Proposition 1C.

- Use publicly-owned land as a means to increase the feasibility of homeownership developments serving a portion of modest-income households. The City and County, CADA and PERS all have the ability to leverage the value of land to include and increase affordable units.

- Finance off-sites with non-housing funds for modest-priced housing
    - SACOG's Community Design Program
    - Jobs/Housing Balance Funds
    - New infill and innovative housing funds through Proposition 1C
    - State transportation and housing funding for transit-oriented development
    - Local public works funds

- Provide parking reductions for certain levels of affordability.

- Participate in new private/public lending partnerships for reduced interest-rate and downpayment assistance grants for moderate-income households.

Conclusion

To quote the Brookings Institution's concluding statement in "Who Lives Downtown?"

"Understanding who lives...downtown is paramount in informing the kinds of housing and investment strategies needed to ensure that downtowns reach their potential to become vibrant, healthy places to live and work."

Downtown's data speaks clearly to the need to increase homeownership levels and to provide a place downtown for modest-income home buyers. Therefore, to increase the City's capacity to stimulate more affordable homeownership downtown, staff recommends that a new modest-income homeownership program be developed incorporating the incentives and financing outlined in this report. Returning homeownership opportunities to this income group is critical for downtown's stability and provides a place for first-time homebuyers downtown.

Therefore, the following Downtown Housing Strategy is recommended:

- Foster market rate development through
  - A positive development climate;
  - Strategic public investments in amenities and infrastructure; and
  - Attention to economic growth, including education resource.
- Invest in mixed-income developments for the downtown workforce.
- Maintain or increase commitments to residential hotel preservation and replacement.
- Develop and implement a modest-income homeownership program.