

The state wants voters to let it get into the lending subsidy game.

California Has a Home to Sell You

Note
California taxpayers have spent tens of billions of dollars on affordable housing to little productive effect. Yet special interests want voters this November to pony up tens of billions more and—get this—establish a state-backed housing lender. Call this the triumph of false hope over experience.

The California Association of Realtors and labor unions are backing Prop. 37, a ballot measure that would authorize the California Housing Finance Agency to issue \$25 billion in government bonds to fund a home down payment assistance program. Another measure (Prop. 1) would authorize \$11.25 billion in bonds to fund affordable housing.

Supporters say the down payment program won't cost taxpayers a dime, but this is misleading. The state would issue bonds to fund loans to cover down payments for buyers of newly constructed homes. Loans could cover as much as 17% of a home's purchase price, so the buyer would only have to put 3% down.

The down payment loan would be a second mortgage, which a buyer would pay off over time. While the program is ostensibly aimed at helping middle-income households, buyers earning up to 200% of an area's median income could qualify for homes costing as much as \$1.5 million. The median is roughly \$400,000 for a family of four in Silicon Valley.

Note
Why is the state program needed given that the federal government already backs mortgages with minimal down payments? The Federal Housing Administration insures mortgages with 3.5% down payments, though borrowers must pay premiums equal to 1.75% of the loan amount, plus a roughly 0.55% annual fee for the life of the loan.

Government-sponsored enterprise Fannie Mae also guarantees mortgages for lower-income households with as little as 3% down, though borrowers generally must pay higher interest rates and insurance premiums. California's program looks to be a subsidy for the relatively affluent who are struggling to afford homes at ethereal prices and today's interest rates. The idea seems to be that the state down payment loan would obviate the higher interest rates buyers would otherwise have to pay under federal programs if they put only 3% down. By making a 20% down payment that is mostly funded by a state-backed second mortgage, borrowers could qualify for a lower interest rate.

It's not clear the state could fund down payment loans at rates that are attractive to borrowers without losing money. The state might be able to take advantage of the municipal bond tax exemption to issue bonds and thereby fund down payment loans at below-market rates. Thirty-year tax-exempt muni bonds currently yield around 5.7%.

Note
But the state would still have to factor in the price of the loan's administrative and underwriting costs. Because the down payment loans would be subordinate to a primary mortgage, bond buyers would likely charge a yield premium. While California might set interest rates on down payment loans below its cost of funding, taxpayers would then be stuck subsidizing them.

Note
In any case, subsidizing buyers will push up prices as long as supply remains constrained. Prop. 1 won't help with either. Most of the \$11.25 billion in bonds would fund homeless and multifamily housing, which can cost \$1 million a unit to build because of government building codes, prevailing wage requirements and other regulation.

California voters have approved \$12 billion in bonds for such projects since 2018, which comes on top of nearly \$20 billion in general fund spending. Yet both homelessness and housing costs have increased. Let's hope voters have the wisdom to stop this endless housing-subsidy racket and defeat both propositions.

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