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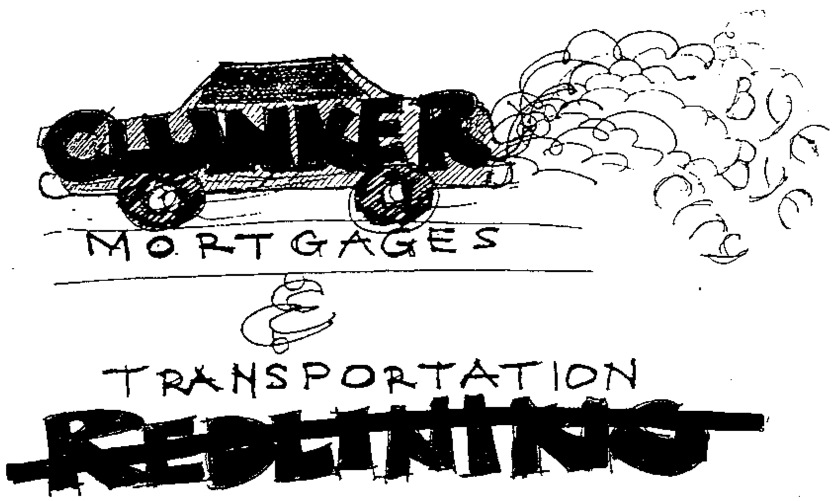
# Clunker Mortgages And Transportation Redlining

*How The Mortgage Banking Industry Unknowingly Drains Cities And Spreads Sprawl*

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**Washington, DC**
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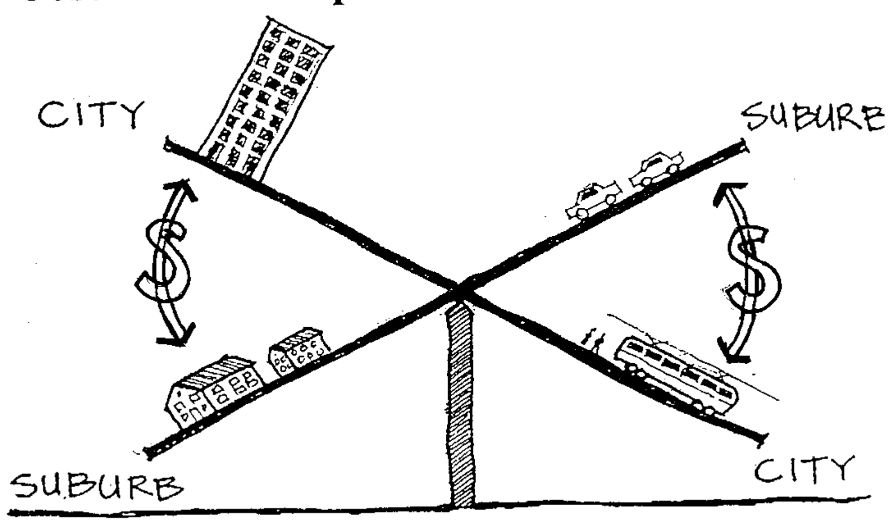
**Introduction**

Urban decline and suburban sprawl have dominated most US communities since World War II. Endless efforts to stop both have been largely unsuccessful. Many people feel the two issues are somehow related. The chain of cause and effect between urban decline and suburban sprawl, however, has never been clear. It may be mortgage approval procedures.

Since World War II, the classic route to affordable home ownership has been a long commute in a clunker. It leads to a suburban neighborhood where two cars are essential.

The cost of a typical car averages $3,000 a year (Hare, 1993, based on FHWA, 1991; and AAA, 1991).(1) That is a large drain on an entry-level buyer's income. It reduces the funds buyers have available to make mortgage payments. On paper, however, it does not. When bankers calculate how much income a buyer has available to meet mortgage payments, they do not subtract car costs. They do not reduce a suburban buyer's capacity to make mortgage payments by the $3,000 a year cost of a second car. Most banks are following rules set by Fannie Mae and Freddie Mac, who buy mortgages from local banks and resell them to investors.

**1.1 The Housing Cost/Transportation Cost Relationship**




City land is expensive because transportation is cheap; suburban land is cheap because transportation is expensive. Inexpensive transportation is the basic reason for cities.

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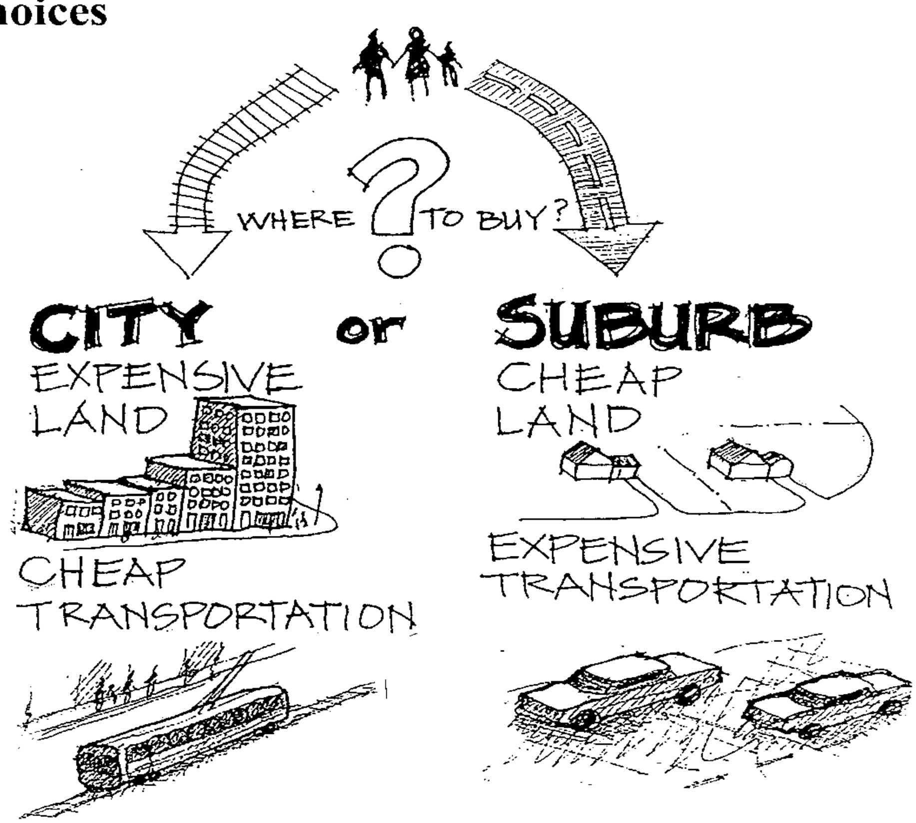
**Ignoring Land Economics**

The mortgage industry unknowingly promotes sprawl and drains cities by ignoring the basic principal of land economics: low land price typically means high transportation costs (see for example Hanson, 1992, citing Wingo, Alonso, Kain, and others). The mortgage industry ignores the low cost to households of urban transportation, as well as the high cost to households of suburban transportation. An example illustrates how.

**1.2 Housing Choices Are Transportation Choices**




The real choice between a city home and a suburban home involves both housing cost and transportation cost.

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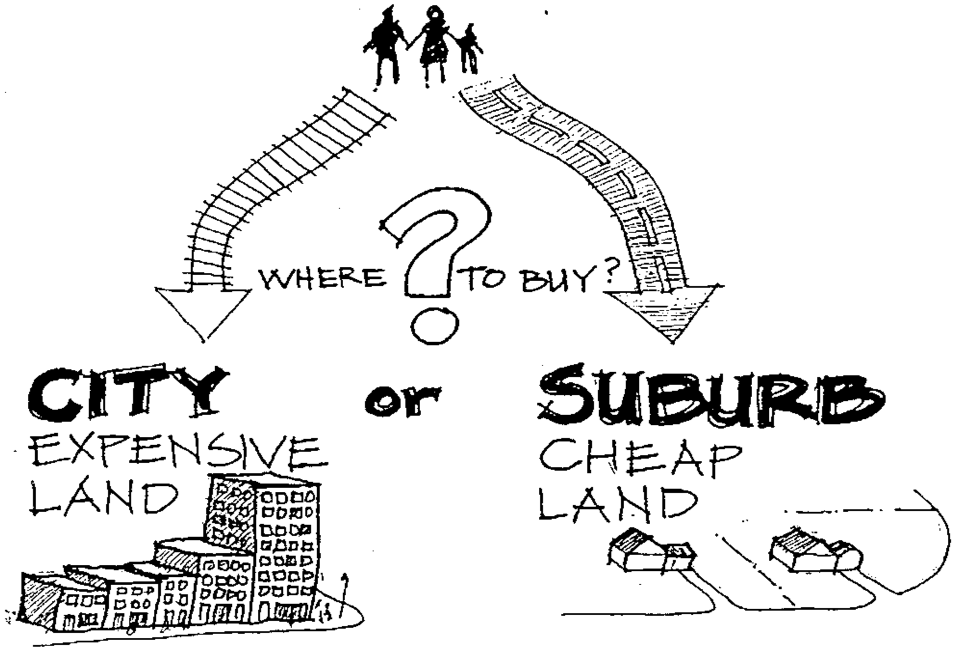
Suppose a couple that wanted to buy a house in a city said to a bank, “Since we live near transit where we don’t need a second car, we will have about $3,000 a year more to make mortgage payments. Will that count as income available to meet mortgage payments?” The bank, reflecting industry standards, would say no.

## 1.3 Mortgage Approval Ignores Transportation Costs




Few households can buy where they can't get a mortgage. It is easier to get a mortgage where cheap land makes house prices low. Mortgage approval procedures do not consider the household's transportation costs at the home that is being bought.

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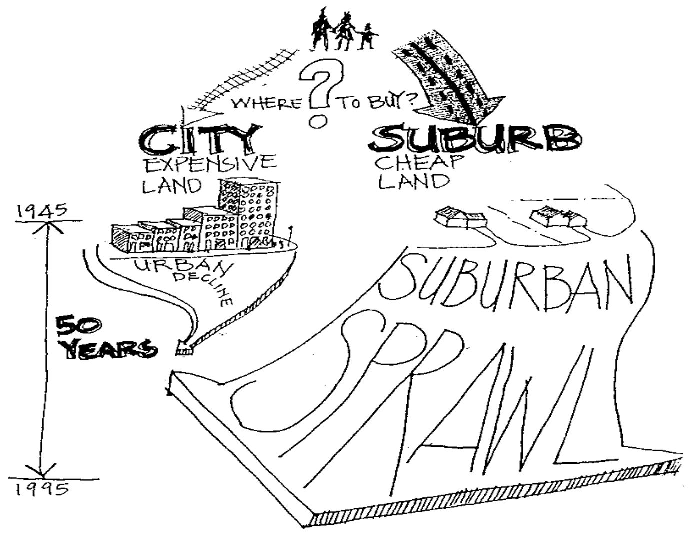
On the other hand, if the same couple wants to spend $3,000 a year of its income on a second car to get a house in the suburbs where two cars are essential, the mortgage bankers have no objections. They don’t reduce their estimates of household income available to meet mortgage payments by the cost of second cars. They do count outstanding car loans or car lease agreements. However, most second cars of entry-level buyers are paid off, and have no outstanding financing or leasing agreements. They are clunkers. In addition, loan and lease agreements only reflect about 40% of total car costs, at most, according to Federal Highway statistics (FHWA, 1991).

In summary, saving $3,000 a year using alternatives to a second car doesn’t help a family get mortgage approval to buy a city home. Spending $3,000 a year on a second car doesn’t hinder a family in getting mortgage approval to buy a suburban home. These facts suggest that bank procedures on how people qualify for mortgages are arbitrary.

## 1.4 Ignoring Transportation Costs In Mortgage Approval Causes Urban Decline And Suburban Sprawl.




**The middle class has left cities for the suburbs since the end of World War II, when US cities and their transit systems were both in good condition. Low down payment mortgages and cars both became widely available immediately after World War II.**

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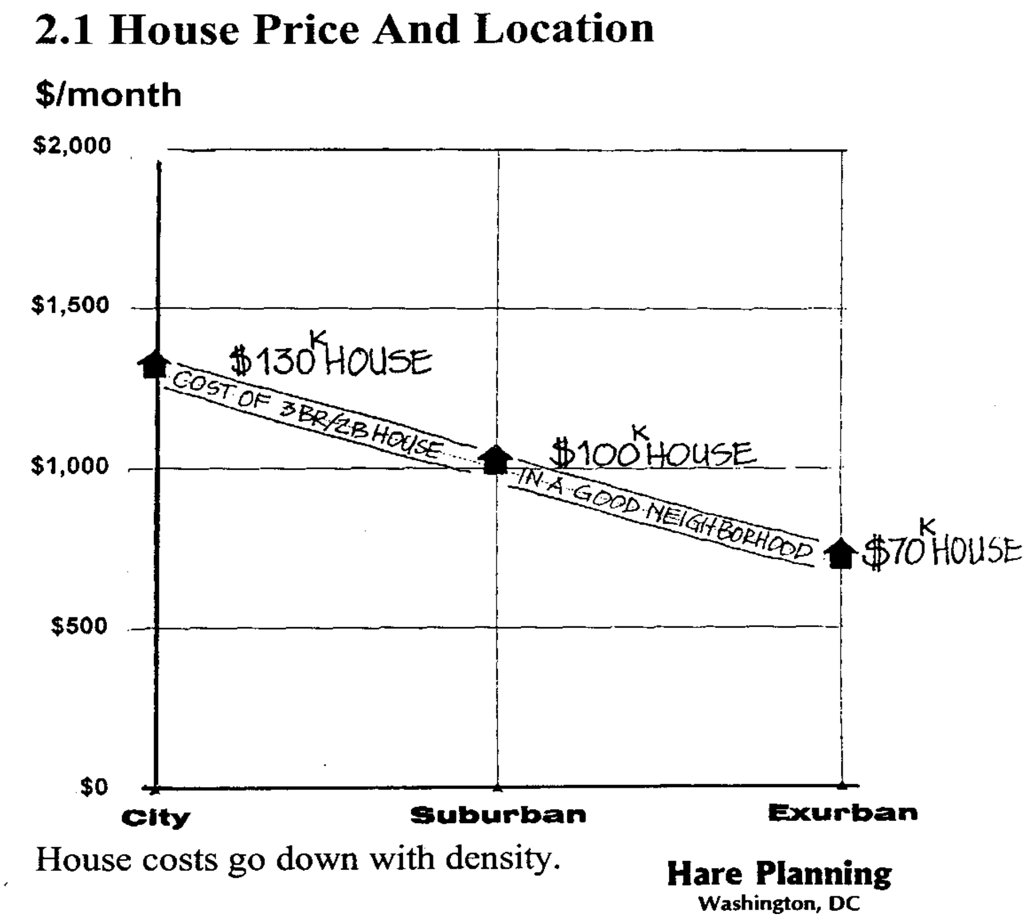
They are arbitrary because they ignore transportation costs. Cheap land makes suburban houses more affordable on paper. In reality those savings are offset by the high costs of second cars needed for suburban living. In the mortgage approval process, however, they are not. Ignoring the two-car cost of suburban living makes suburban buyers look as though they are spending less on housing then they are. It ignores the fundamental relationship between land price and transportation costs. Suburban homes are cheap because the transportation to them is expensive.

Seen in this light, it is easy to understand why we have suburban sprawl on cheap land, and drained cities. Suburban homes are more “mortgage affordable” because no one is counting car costs. Suburbs attract buyers while cities lose them because mortgage affordability controls home sales to the middle-class. Mortgage approval is the same as ability to buy for most entry-level middle-class buyers. If you can’t get a mortgage, you can’t buy a home. In this light, a long commute in a clunker is simply a way to spend money on housing without having it counted in the mortgage approval process, or more specifically, in the 30% of income banks typically permit buyers to spend on monthly mortgage payments plus taxes and insurance.

Banks consider cheap suburban land costs, but not high transportation costs, even though elementary land economics says the two are fundamentally linked.

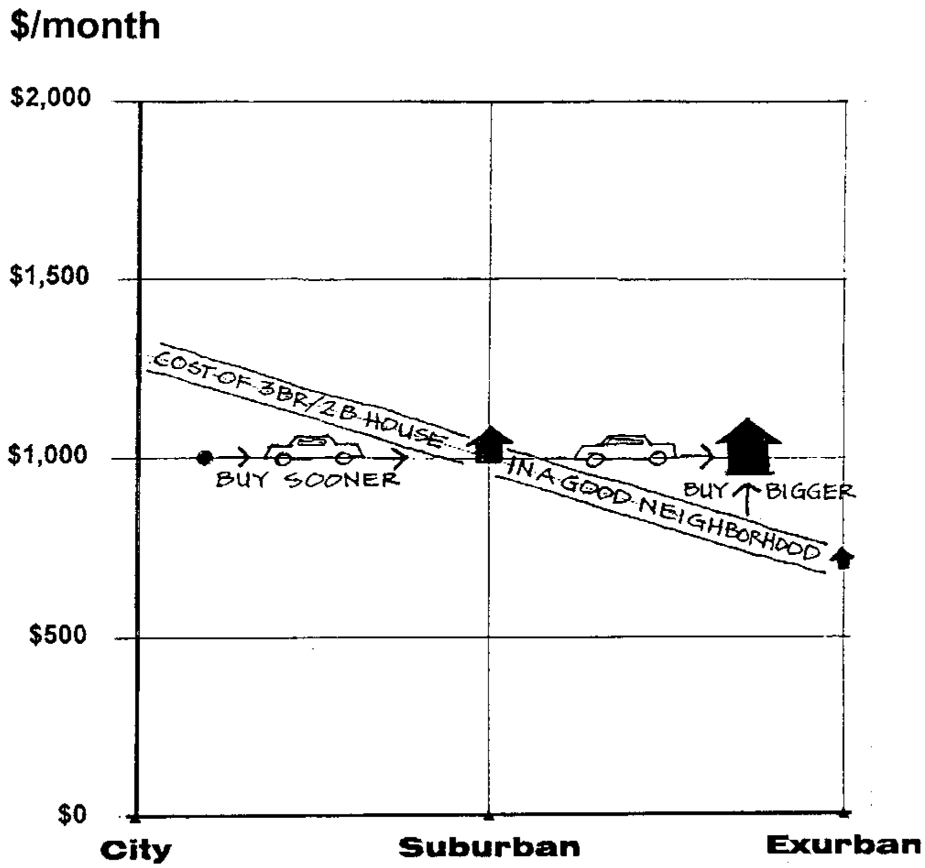



**The 30% Tilt Against Cities in Mortgage Lending**

How much is the affordability of homes affected by the clunker mortgage system? As noted earlier, $3,000 is the typical net savings from giving up an average second car for transit and occasional car rental. Three thousand dollars a year will finance about $30,000 in mortgage money in mid-1995 interest rates. That is a 30% increase in the affordability of a $100,000 home with no subsidy.

In other words, by ignoring the transportation savings from density, mix and transit, the mortgage banking industry reduces the affordability of a $100,000 entry-level urban home by 30%. Another way to make the same point is to say banks increase the affordability of suburban homes by 30% by not deducting second car costs from income available to make mortgage payments. Either way, there is a 30% anti-urban, anti-transit tilt in the home buying process.

## 2.2 Sooner And Bigger In The Suburbs




An entry level middle class homebuyer who lives in the city can get mortgage approval to buy a house sooner, and buy a bigger house, or both, by moving out of the city.

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**The Urban Leadership Drain**

Clunker mortgages affect more than just the affordability of housing, however. By attracting most entry-level buyers to the suburbs, they shrink demand for urban middle-class neighborhoods. The number of middle-class neighborhoods then shrinks to meet the shrunken demand. A surplus of affordable middle-class homes exists in most cities, but it is mostly in neighborhoods which middle-class buyers of all races now find unacceptable in terms of schools and crime.

The false affordability of the suburbs drains entry-level buyers and the urban residential tax base and neighborhood leadership and finally neighborhood stability. This doesn't happen all at once. It happens over time, essentially over the time since World War II.

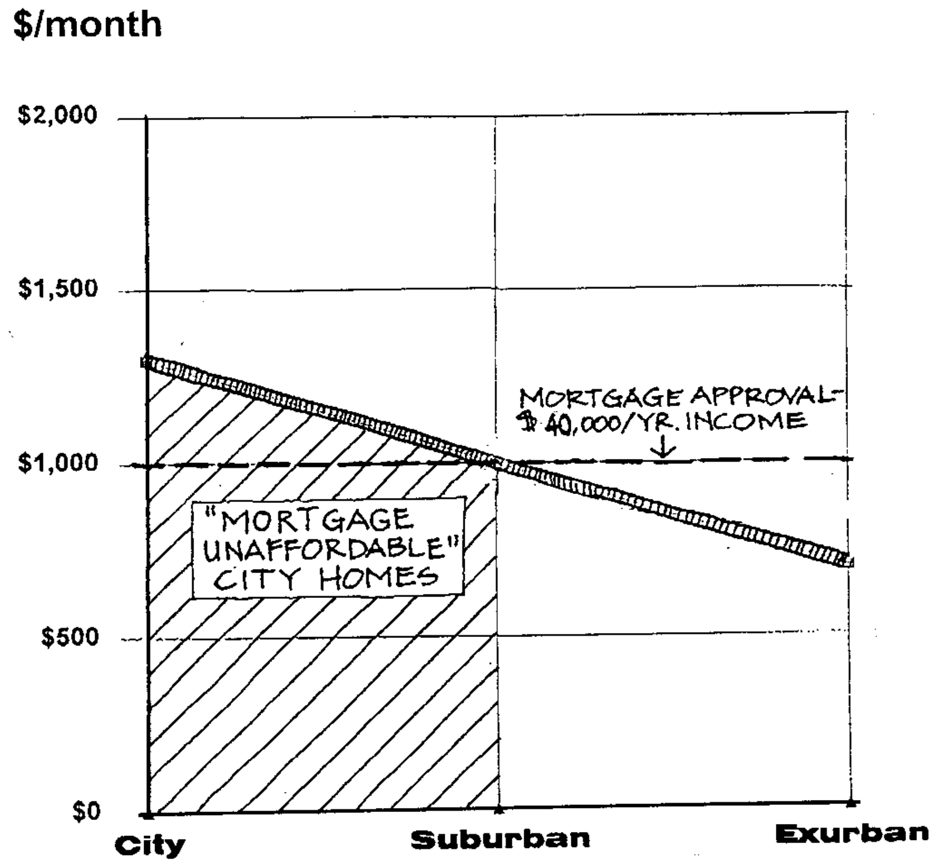
At the end of the War, US cities where still in good condition, and typically had good schools. Many rural and suburban children were sent to urban schools because they were better. At the end of the war widespread availability of both low down payment mortgages and affordable cars combined for the first time. Over the 50 years since World War II, the 30% tilt of mortgage approval practices against urban homes has compounded like interest payments into the huge problems associated with most American cities. It has drained neighborhoods of the majority of the young leaders who run PTAs and Scout troops and Little Leagues and block associations. Those who stay are overburdened, and typically fight a losing battle. The result has been growing social disorganization, growing flight of the middle-class of all races, worse problems, and widespread prejudice against city neighborhoods, again among people of all races.

In many observers' thinking, the historic lack of civil rights for minorities has been a direct cause of urban crime and violence since World War II. However, the causal link is no longer as clear today as it once seemed. For the author, it was weakened by hearing a black suburban resident swear he would never come back to the city again because of the crime and violence.(2) He had voted with his feet and with his family.

From his point of view, neither civil rights nor affirmative action would solve urban problems. It is also worth noting that the poverty and indignity caused by pre-war racial discrimination does not seem to have led to the kind or severity of urban problems like the ones we have today.

White flight may not have been as white as it seemed. It is possible that the overwhelming attention to race in US society since the civil rights movement blind us to other causes of social problems. White flight, particularly in the years following the 1968 Fair Housing Act, may have become middle-class flight by all races. In any case, prejudice against city neighborhoods among all races now helps the clunker mortgage system drain cities of their middle-class.

## 2.3 "Mortgage Unaffordable" Homes




Banks typically allow 30% of income to be spent on housing. Since 30% of $40,000/yr is $1,000 a month, the middle class can't afford middle class city homes.

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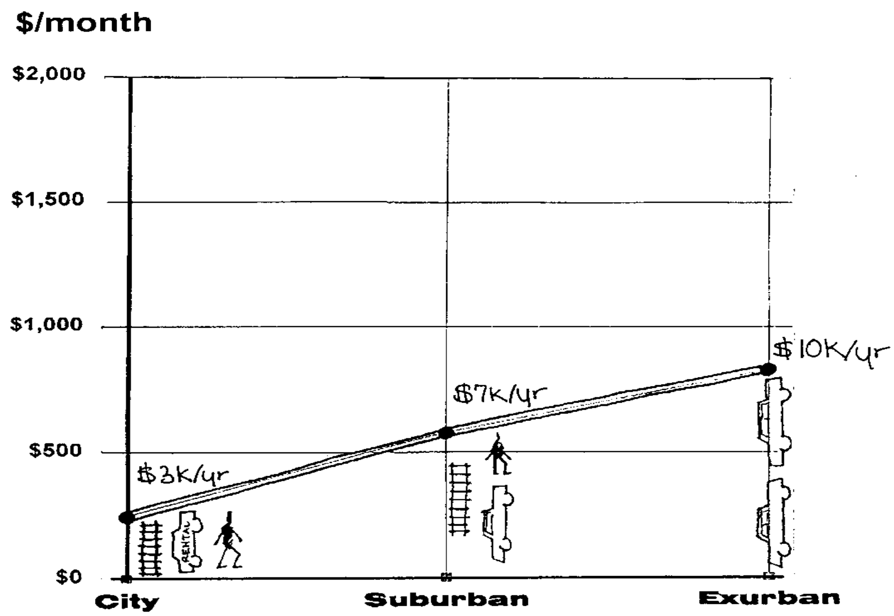
**The "Divide and Hide" Way We Pay for Cars**

The way we pay for owning and operating cars helps in the deceptive affordability of suburban homes. We pay for cars through a "divide and hide" system that turns household car costs into a fine mist we sense but cannot measure, like tiny droplets of fog on a dark night. Some payments are made daily or weekly, some monthly, and some annually, for things as diverse as gas, oil, insurance, tires, tolls, repairs, depreciation, parking, loans or lease payments, registration, etc. Almost nobody adds up the totals. Few transportation planners, or banks, or households recognize that most two car suburban entry-level homebuyers spend more than 20% of their yearly budgets on cars (Bureau of Labor Statistics, 1991).(3)

**Thirty Percent May Be A Conservative Estimate Of The Tilt Against Cities**

Many people live in cities without any cars. What if instead of two cars, an urban household has no car and uses a combination of alternatives such as walking and bicycling and rollerblading and transit and car rentals and trains? Then the argument that current mortgage procedures create a 30% affordability tilt towards the suburbs is very conservative. The National Resources Defense Council, in a paper by John Holtzclaw, says the average annual savings from living where few cars are necessary is $5,000 in savings (Holtzclaw, 1995). That figure suggests a 50% mortgage approval tilt against a $100,000 entry-level city home. Since Holtzclaw's figure is an average for people who live in high density neighborhoods, the figure for middle-class households who do not own an automobile is probably higher, something like $7,000 (Hare, 1994)

**2.4 Transportation Cost And Location**




Although house prices go down in suburban areas, transportation costs go up.

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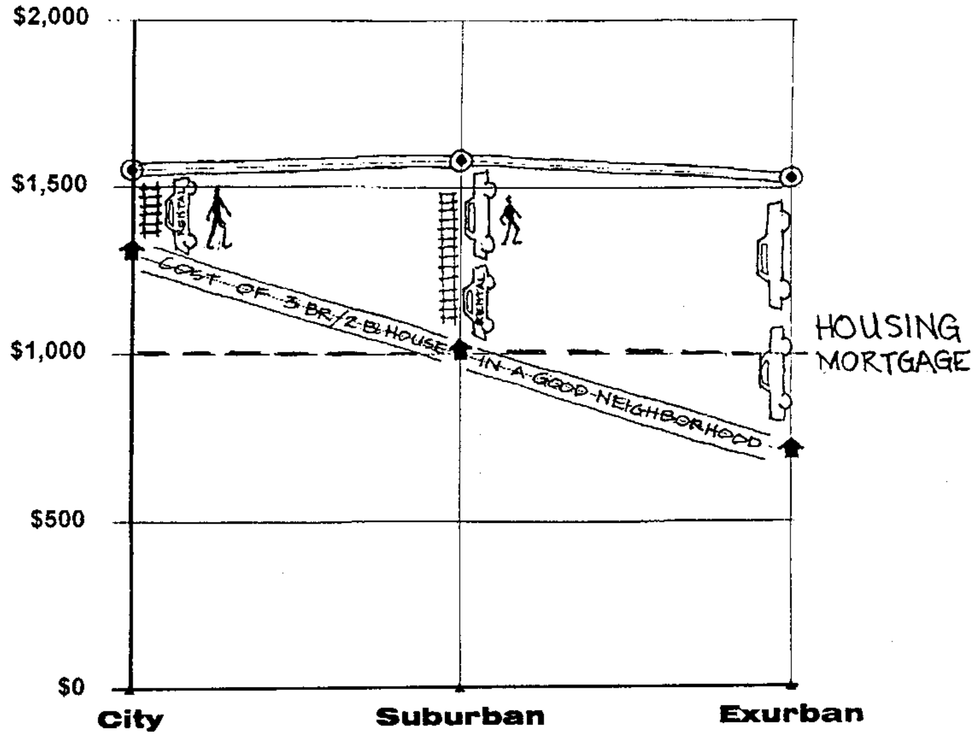
# 2.5 Housing Plus Transportation Costs




Increases in transportation costs in the suburbs and exurbs eliminates the monthly savings from buying lower priced suburban and exurban homes.

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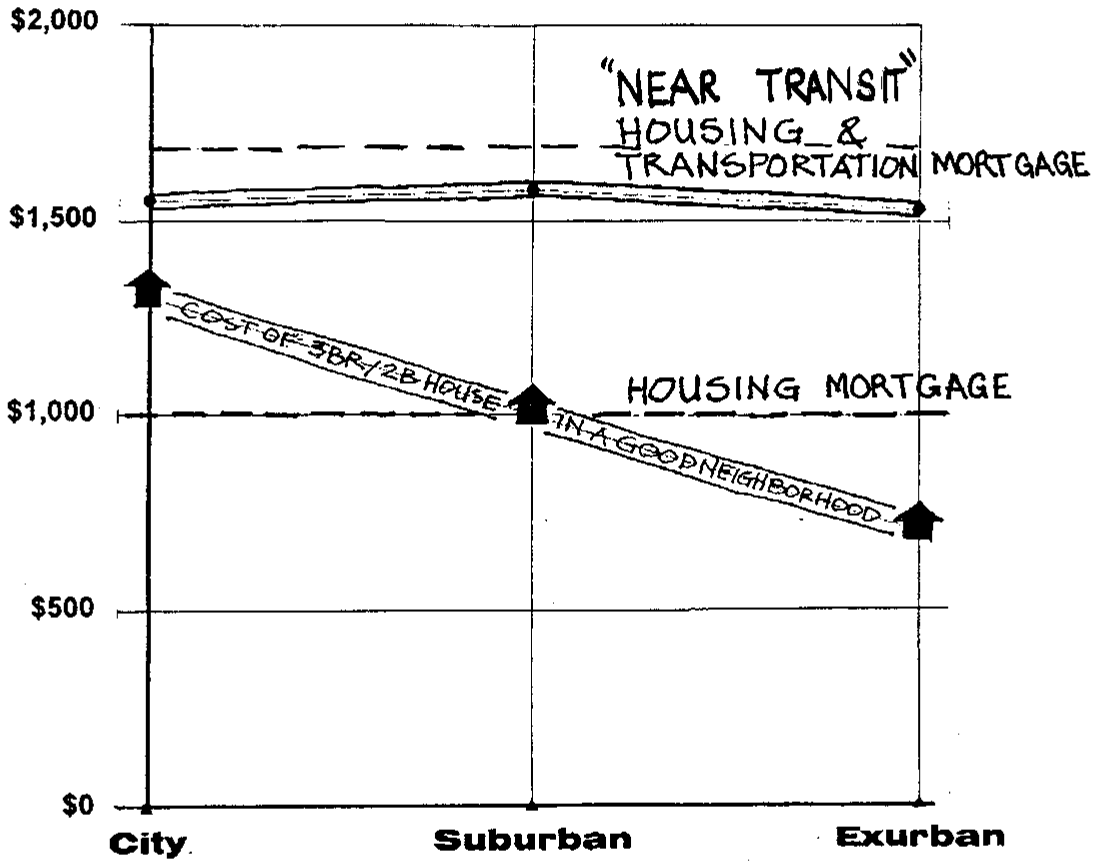
# 2.6 Housing & Transportation Mortgaes




If mortgage approval procedures reflected the combined cost of housing and transportation costs, city homes could compete equally for entry level middle class homebuyers.

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**The Solution is Near Transit Mortgages, Or One-Car and No-Car Mortgages**

If in fact mortgages procedures are a major contributor to urban decline and suburban sprawl, there is a simple solution. It is larger mortgages for people who spend less on transportation, which essentially means spending less on cars. One-car households have more money available to meet mortgage payments, so they should get bigger mortgages. The mortgages should be "one-car mortgages" or "no-car mortgages" or "near transit mortgages." (Hare 1993, 1994). The National Resources Defense Council prefers "location efficient mortgages" (Holtzclaw, 1994). The remainder of this paper will use the term, "Near-transit mortgages." Near transit or one-car mortgages would get cars off the road, and make housing more affordable, at the same time, at no public cost. That point bears repeating. Near transit mortgages would address two major issues, congestion and the cost of home ownership, simultaneously and with out subsidy.

Near transit mortgages raise two problems in many people's minds. They are enforcement of reduced car ownership among homebuyers, and reorienting the mortgage banking system. Both are mechanical problems that are simpler to solve than they seem. Although too technical to discuss here in detail, they are addressed in *Making Housing Affordable by Reducing Second Car Ownership* (Hare, 1993). It is possible to create near transit mortgages without reforming the whole mortgage system right away. They can be made with local housing funds, or through second mortgages, or through public or private mortgage insurance.

Enforcement of reduced car ownership for near-transit mortgage holders raises the old question, "Will Americans get out of their cars?" In fact, it is not the right question. The right question is, "Which Americans will get out of which cars first?" Americans will get out of second cars first, and the first ones to do it will be those for whom the cost of the second car, $3,000 per year, is a large part of their disposable income.

The marketing strategy is then fairly simple. First, through near-transit mortgages, harness something people really want, like home ownership, to the financial incentive to give up cars. It was the desire for home ownership that got so many of us into multiple car ownership in the first place. Second, don't pretend transit is an automatic substitute for a car. Focus on marketing cars for what cars do best, and on transit for what transit does best.

**Car Ownership Can Be Reduced By Maximizing the Savings From Giving Up Cars, and Minimizing The Inconvenience**

Many people say they cannot live without two cars. Many probably can't, especially right away, but we don't need to give up all cars, or even most cars, all at once. Getting rid of 5% or 10% of cars, particularly the clunkers that pollute, would be a huge stop forward. Because highways move from capacity to congestion with the addition of relatively few extra cars, marginal reductions in traffic have a disproportionately large effect on reducing congestion. Transportation policy generally does very little to help us even think about reducing car ownership. The term is not even part of the transportation profession's jargon.

Most transportation policy is based on the premise that transit is as good as a car. It is in fact better than a car, but only from the public policy point of view. From a transportation consumer's point of view, transit is rarely as good as a car. Cars are much faster than transit, and better for weather, comfort, security, parcels, and privacy when traveling with others. That is why taxis can compete effectively with the world's best transit systems. Almost the only private benefit to taking transit is the savings over not owning a car. They are substantial. However, instead of marketing that benefit, transportation planners try to convince people that they should leave their cars at home and take transit because it is as good as a car.

It rarely is. Leaving a car at home to take transit typically means paying for the car, and paying for transit, and paying again in lost time and convenience, security, privacy, weather protection, and parcel carrying.

Transit agencies could emphasize these potential savings in their marketing efforts. If a household gives up a typical second car for transit, it saves the equivalent of about $12 an hour for the extra time a household member spends on commuting (Hare, 1995).

Transit is not the fastest way to work, but for many people it is the fastest way to the bank. The main reason to ride transit is the dramatic savings over car ownership. Once that is recognized, transportation planning is simpler. It can focus on maximizing the savings and minimizing the inconvenience of not owning second cars, or in some cases, any car.

The simplest strategy is probably just to educate households about how much their cars cost them through a transportation cost guide to home buying, or "True House Price Guide." It would show home buyers how buying into an exurban, two car home means buying into a $7,000 a year transportation habit for as long as they own their home (Hare, 1995).

A second strategy is to promote neighborhood car rental. Neighborhood car rental makes it easier to give up a car, because there is a car easily available when nothing else will do, at far less than the cost of car ownership. (Hare, 1995). A third strategy is to promote take home shopping carts, and have retailers subsidize them just as they do parking. A shopping cart is basically a pedestrian station wagon, except that, unlike a four wheeled station wagon, you can't drive it home.

The frequent theft of shopping carts, in rich neighborhoods as well as poor ones, provides evidence that take home shopping carts are a good solution to carrying parcels without a car. These and other strategies for minimizing the inconvenience of now owning second cars, or in some cases first cars, are detailed in Planning, Transportation, and the Home Economics of Reduced Car Ownership (Hare, 1995).

### Shifting Demand Back To The Old Neighborhood

Such strategies would make near transit or one-car and no-car mortgages more feasible. In fact, reflecting the true costs of transportation in decisions about where to buy a home would shift home buying preferences toward places which maximize the savings and minimize the inconvenience of reduced car ownership.

Older neighborhoods were designed for one-car and no-car households. Near transit mortgages would shift home buying preferences away from suburban sprawl, and back towards cities, small and large. Rural cities would be helped in efforts at revitalization, and new suburban centers themselves would tend to be more concentrated. Near transit mortgages would shift preferences back toward higher density neighborhoods, and back into transit. Over time, near transit mortgages would improve the market for city homes dramatically, along with city tax bases, the stability of city neighborhoods, and transit ridership. They would create consumer demand for new neighborhoods built so that households could live in them with fewer cars. Near transit mortgages would make a strong contribution to stopping both urban decline and suburban sprawl.

Advocates for urban preservation, rural preservation, the environment, transit and affordable housing should request that the mortgage industry reform its mortgage approval regulations. So should people who support free markets and capitalism, because mortgage approval regulations are a good example of how bad regulations distort markets.

In summary, this paper argues that a mortgage approval system ignores the basic principle of land economics has contributed heavily to suburban sprawl, reduced transit ridership, loss of urban population, and loss of leadership of all races in urban neighborhoods.

The clunker mortgage system unknowingly creates the false affordability of the suburbs. It blinds households to the basic economics of human settlements at the very point at which households are deciding where to settle. Mortgage approval should take into account both housing and transportation costs.

### Endnotes

1. This figure is developed in Hare 1994. It is based on the Federal Highway Administration's Cost of Owning and Operating Automobiles, Vans, and Light Trucks 1991, and the American Automobile Association's Your Driving Costs, 1991 Edition. Transit and car rental costs have been netted out. Transit was estimated at $4 a day for 250 working days, and car rental for 12 days at $25. The figure is conservative.

2. Personal experience of the author, September 1994. The man had come back to his converted van from visiting a relative in a Washington DC hospital. His passenger window had been broken and his radio had been stolen.

3. According to BLS Consumer Expenditures data, households in the second expenditure quintile spend an average of 15% of their income on cars, and households in the third quintile spend 17% of their income on cars. If no car and one car households in these groups are taken out, the average in both groups for two car households would be over 20%.

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# Planning, Transportation, and the Home Economics of Reduced Car Ownership

planning as if
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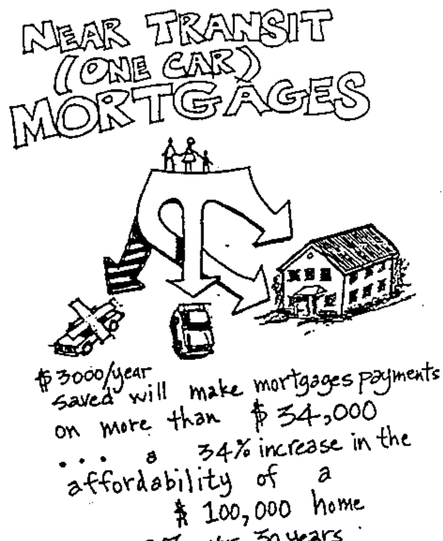


topics:
* JUNKING THE CLUNKER
* ONE CAR MORTGAGES (NEAR-TRANSIT MORTGAGES)
* ONE CAR RENTS
* TDM FOR HOMES AND SHOPPING
* THE MIS-MARKETING OF TRANSIT
* BIKES ARE FASTER THAN TRANSIT
* GLUING TOWNS TOGETHER ACROSS ARTERIALS
* ONE CAR CENTERS
* PETER PAN SUBURBS
* REVITALIZATION FROM NEAR HOME SHOPPING
* TRAIL AND TRANSIT "AVENUES WITHOUT AUTOS"
* THE NON-MARKETING OF OLDER NEIGHBORHOODS

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# Review Comments on *Planning, Transportation, and the Home Economics of Reduced Car Ownership*

"This is not a small subject. Pat Hare's book is at the heart of much of what is wrong with our society" **Andres Duany**, the nation's leading urban designer and designer of Kentlands, MD and Seaside, Fla.**** "He knows the problems, he has the solutions…he has the ability to help us understand them easily."**Dwight H. Merriam,** past president, American Inst. of Certified Planners **** "95% of the material in this book is not in any other publication." **Perry Berman**, Chief, Community Planning, Montgomery Cty. (MD) Planning Board **** "His ideas are novel, seem workable, and don't require taxpayer subsidies." They are, "...from a knowledgeable source." **Planning Magazine** **** "Transit, cars, and bikes -- it all finally makes sense! No one analyses the numbers -- and the wrong assumption we've been struggling under in our cities and suburbs--as well as Pat Hare. This presentation was a revelation. " **Peter Harnik**, VP for Trail Development, Rails To Trails Conservancy. **** "A fascinating book of ideas and projects." **Tony Hiss**, Staff Writer, The New Yorker **** There was tremendous enthusiasm for your presentation. In particular, people appreciated the unintimidating quality and humor of your visuals." **Anne Pearson**, Annapolis Summit. **** "Thank you for your excellent slide presentation. I heard many candid comments indicating it was the highlight of the conference." **Kristin Pauly**, Chesapeake Bay Foundation. **** "Turned our thinking on its head." **Paul Massicot**, Director, Tidewater Administration, Maryland Department of Natural Resources. **** The concept graphics make it easy for planning commissioners and busy people to skim through the book, get the essence of its innovative ideas, and read the detail only where they choose. And the ideas themselves are relevant and timely: the 'mis-marketing of transit,' how to reduce parking lot size while attracting new customers, and many more ." **Wayne Senville**, Planning Commissioners Journal.. **** "The amusing graphics are a powerful communications tool. The material avoids, 'planner-speak'." **Bill Clarke**, Legislative And Commuter Sub-committees, Maryland Bicycle Advisory Committee. **** "A pragmatic visionary." **David Kahn**, Architecture and Planning , UC Boulder. ****"…shows how the household cost of cars can be used as a very powerful tool to change travel habits, and applies this tool in many surprising new ways." **Don Chen,** Surface Transportation Policy Project **** " His ideas should be applied in every community." **Todd Litman,** Victoria(BC) Transport Policy Institute**** "He is one of the very few people who is thinking creatively about reducing car ownership, and about how and when it is in many household's personal self-interest to own fewer cars" **Jeff Blum,** Transportation Policy Director, Citizen Action **** "Complexity in planning and transportation is often just an excuse for lack of clear thinking. This book not only presents very clear thinking, but presents it in graphics that can be slapped onto a copier, made into transparencies, and used to communicate with others. It is very unusual, in that it is anti-sprawl, without being anti-automobile." **Sandy Hillyer**, National Growth Management Leadership Project. **** The format, and the ability to use the seminar book's graphics for our own community presentation, makes the book unusually valuable. **Susan Osborne**, Planning Department, Boulder, CO.

## *A Few Of The Unusual Points Documented In* **Planning, Transportation, and The Home Economics Of Reduced Car Ownership**:

- There are two ways to make housing more affordable, and get cars off the road, at the same time, and at no public cost : <u>bigger mortgages</u> for people who can make bigger mortgage payments because they own only one car, or no car. The increase in purchasing power would be from $30,000 to $70,000 dollars; and <u>lower rents</u> for people with no car. The cost of a “free” parking space is about $50 a month, a 10% reduction on a $500/month rent).
- No transit agency ever markets the best reason to take transit: You can pay yourself $12 an hour for the extra time spent commuting by transit, because if you give up a second car for transit, bikes, and car rental, you save $3,000/year ($3000 year saved/250 extra hours commuting = $12 saved per extra hour commuting).
- Bikes are faster than rail transit, and almost twice as fast as local buses; the combination of bikes, rental cars, and transit together are an effective cost & convenience competitor to cars, and should be marketed together.
- Ninety-five percent of the suburban landscape is bicycle friendly; the suburban challenge for biking is less finding trails than finding “bridgers” over, under and around the arterials and the freeways. They cut the suburbs up into separated islands without safe connections for cyclists and pedestrians; many “bridgers” already exist but are not publicized or mapped.
- Greenways from suburbs to central cities, new avenues without autos for transit and trails, could easily be built in most major cities.
- The marketing for almost any product is better than the marketing for old neighborhoods.....because there isn’t any marketing for old neighborhoods. Unlike new neighborhoods, old neighborhoods are marketed in the small print of the classifieds, house by house, with no description of the neighborhood or its qualities… even though older neighborhoods are often better planned, and have more amenities, and more homes for sale, than most new subdivisions.
- Reducing car ownership is the best way to revitalize older shopping areas.
- About half of all free parking is a waste of retailers’ money: 30% percent of retail parking spaces are used less than 100 hours a year.
- The growth of neighborhood car rental will probably do more for the environment than any effort to fight highways and build transit.

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# Hare Planning

## *Firm Background and Qualifications:*

Mr. Hare started the firm in 1981, concentrating on accessory apartments, and "granny flats." Accessory apartments provide affordable rental housing, integrated into good neighborhoods, at no public cost. They also make home ownership affordable, and help older people age in place. The firm has been recognized in the US and Canada as a leader in this area. The **National Journal** has called Mr. Hare, "the nation's leading champion of accessory units." His books on the topic are recognized as the leading publications in the field. He is also known for his work on the problems of aging in place in post-war suburbs.

From 1983 to 1991, Mr. Hare worked part-time with the Maryland-National Capital Park and Planning Commission(the Montgomery County(Maryland) Planning Department. While still maintaining his consulting practice, he had major responsibilities, including preparation of an award winning master plan for an older suburban area, and running a major growth management study and an innovative HOV design project. This work led to original proposals and concepts, including, **One Car Mortgages, One Car Rents, The Mis-Marketing Of Transit, One Car Centers, Revitalization From Near Home Shopping, Gluing Towns Together Across Arterials, Trail And Transit Avenues Without Autos, Remarketing Of Older Communities, etc.** Comments on the firm's recent publications presenting these ideas include, "...filled with innovative and practical concepts and visions for planners, elected officials, and activists...(Michael Replogle, Co-Director, Transportation Project, Environmental Defense Fund) "Fills a real gap on how to make neighborhoods affordable to households and society at the same time."(John Holtzclaw, Chair, Transportation Subcommittee, The Sierra Club) "His ideas are novel, seem workable, and don't require taxpayer subsidies." They are, "...from a knowledgeable source..."(Harold Henderson, Book Reviewer, Planning Magazine) "Pat Hare's book is at the heart of much of what is wrong with our society. " (Andres Duany, DPZ Architects and Planners)

The firm's clients have included the American Association of Retired Persons, The Ministry of Housing of the Province Of Ontario, The Department Of Housing And Urban Development, The US Administration On Aging, the Department of Housing And Community Development of California, many universities, and communities from Seattle and San Diego to Somerset County, New Jersey and Newton, Massachusetts. Mr. Hare is known as an excellent, entertaining speaker.

The firm's work is characterized by pragmatic innovation.

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