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FOCUS ON: SAN FRANCISCO, CALIF.

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San Francisco's scenic views, temperate climate and eclectic cultural offerings have long made it a desirable place to live, but it comes at a high price. San Francisco was ranked the nation's least affordable metropolitan area in 2013 by the National Association of Home Builders/Wells Fargo Housing Opportunity Index, with only 16 percent of its homes affordable to those earning the area median income.

"The market-rate housing price situation is out of control," said David Schnur, director of housing development at San Francisco-based Community Housing Partnership. "The unusual spike has made it so that not only low-income, but also moderate- and above-moderate-income individuals are finding it impossible to find affordable housing."

High-paying tech jobs in the South of Market district are often blamed for driving up housing prices and widening the affordability gap for the majority of residents, but San Francisco housing experts say that's only one piece of the puzzle. On the supply side, other factors include dissolution of the state's redevelopment agencies, shortage of public housing funds, lack of greenfield space and an aging public housing stock in great need of rehabilitation.

About San Francisco

San Francisco is a consolidated city-county that squeezes nearly 826,000 people into an area of less than 47 square miles. The city anchors the San Francisco-Oakland-Hayward metropolitan statistical area (MSA), which consists of San Francisco, Alameda, Marin, Contra Costa and San Mateo counties. While San Francisco is known for being the home of technology companies such as Twitter, Yelp, Craigslist and Salesforce.com, its largest employers are in the government and education sectors. In the private sector, major employers are in the healthcare, finance, retail and science/technology industries.

Although the MSA's unemployment rate rose to 10.3 percent in 2010, employment has recovered faster than the nation overall. As seen in the following charts, the MSA's median household income has also increased significantly, from \$61,155 in 2000 to \$73,042 in 2013. Novogradac & Company LLP projects the MSA's median household income will hit \$85,699 by 2018 — an annual growth of

| YEAR | Median Household Income | | | |
|------|--|---------------|-------------|---------------|
| | SAN FRANCISCO-OAKLAND-HAYWARD, CALIF. MSA | | USA | |
| | AMOUNT | ANNUAL CHANGE | AMOUNT | ANNUAL CHANGE |
| 2000 | \$61,155.00 | - | \$42,164.00 | - |
| 2013 | \$73,042.00 | 1.50% | \$51,321.00 | 1.60% |
| 2018 | \$85,699.00 | 3.50% | \$59,597.00 | 3.20% |

Source: ESRI Demographics 2013, Novogradac & Company LLP, December 2013

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3.5 percent, compared to the nation's 3.2 percent expected annual growth rate.

Housing Market

The city's rental vacancy rate dropped from 6.4 percent in 2009 to 2.8 percent in 2012, reflecting the growing housing demand, according to a report by the city's budget and legislative analyst. Zillow.com estimates demand has pushed the citywide median rental rate for all homes to \$3,400. That means a household's annual income would need to be more than \$136,000 to afford the median rent (and dedicate no more than 30 percent of income to housing costs), according to the Mayor's Office of Housing and Community Development.

"Housing is unbelievably expensive in a scary way," said San Francisco City Supervisor Scott Wiener. "Rents are through the roof, purchase prices are through the roof and there a lot of people who are in unstable housing situations." To help increase the housing supply, Wiener recently introduced legislation for a pilot program that would allow homeowners to build in-law units within the existing footprint of their houses.

Some neighborhoods in particular have seen an increased demand for housing. Cynthia Parker, president of BRIDGE Housing, said BRIDGE's new 60-unit Natoma Family Apartments in the South of Market had 3,000 prequalified applicants. Other neighborhoods in high demand include the Castro, the Mission, the Haight, Hayes Valley, Cole Valley and Pacific Heights.

Wiener said one of the biggest issues affecting the limited housing supply is the rising number of evictions under the Ellis Act, a state law that allows property owners to take their buildings off the rental market—even rent-controlled units. Some protest that the Ellis Act drains the city of its rent-control stock. Others blame strict rent control policies for making Ellis Act conversions more attractive to property owners in the first place. They argue that property owners can profit more by taking their rent-controlled buildings off the rental market than by continuing to lease to tenants who pay rents far below market rates.

Barriers to Entry

Developers agree that their biggest challenges are the high costs of land, entitlements, construction and labor. "San Francisco is incredibly supportive to developers and the affordable housing community, but it's still a tough town to develop in," said Parker, who added that BRIDGE Housing's development costs per unit in San Francisco are about \$560,000 — more than double the \$220,000 average it spends on its Southern California units.

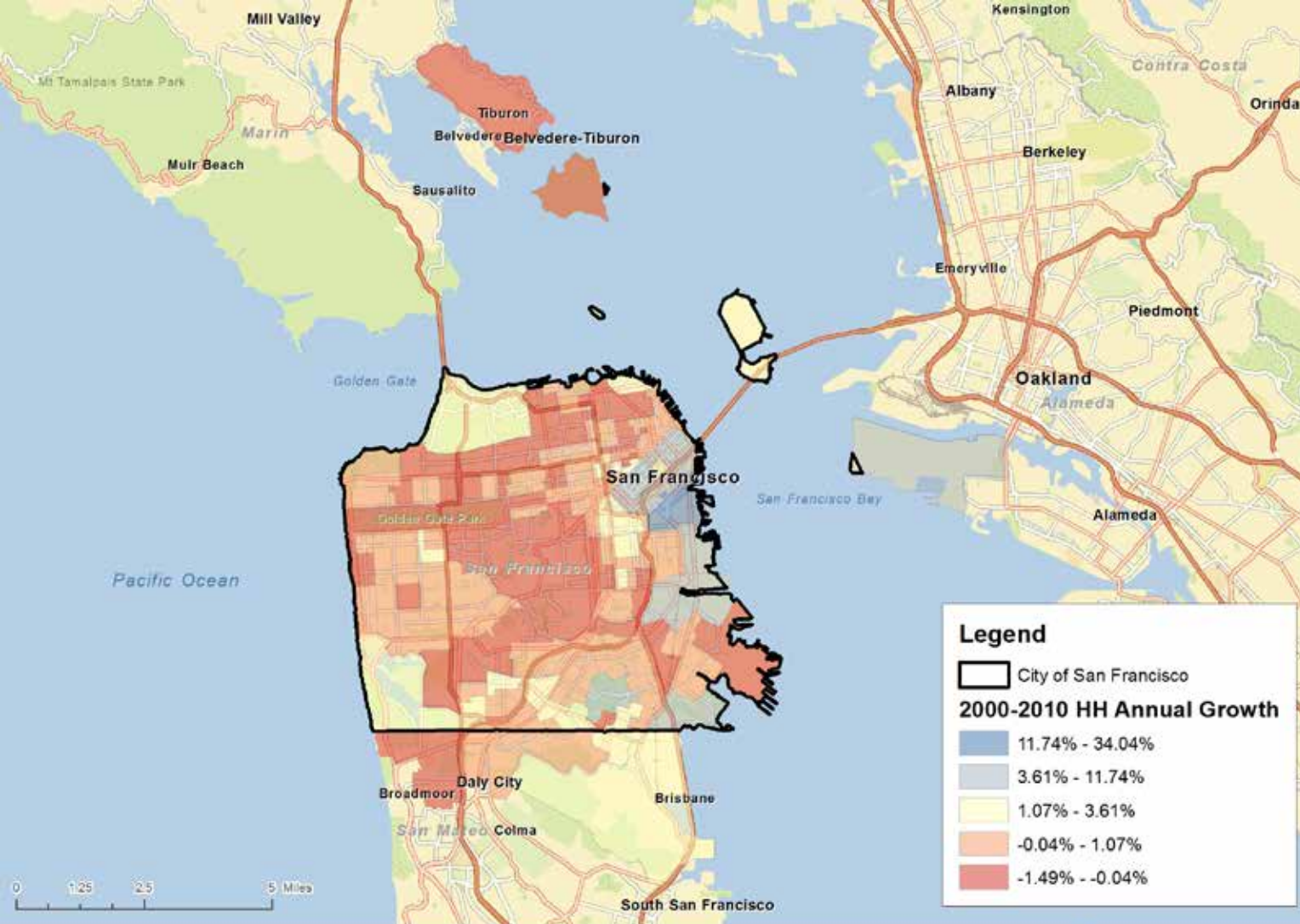
A lengthy entitlement process adds to the expense and uncertainty of developments, said Katie Lamont, director of housing development at Tenderloin Neighborhood Development Corporation (TNDC). Lamont said that while suburban developments can go through the entitlement process in about four months, San Francisco developments could take up to one year or longer.

Another consideration is neighborhood support. "San Francisco has a strong base of community developers and nonprofit organizations that are closely tied to the neighborhoods they work in," said Schnur. He said new developers trying to enter the market will likely find it difficult unless they "make strong and genuine connections to the existing community." Schnur explained that developers must "run the gauntlet of the neighborhood" because San Franciscans are vocal about what type of developments they want in their communities.

The Low-Income Housing Tax Credit and Other Resources

The low-income housing tax credit (LIHTC) is a mainstay of affordable housing funding in the city. "San Francisco has fairly consistently brought in five to nine applications annually during the last 10 years, averaging about seven awards annually. Approximately two-thirds of the awards in the last 10 years have been tax-exempt bond, 4 percent projects," said Bill Ainsworth, spokesman for Treasurer Bill Lockyer, who chairs the California Tax Credit Allocation Committee. Ainsworth said that San Francisco receives 4 percent of the state allocation remaining for geographic regions after set-asides are capitalized, a percentage that he said will be reduced to 3.7 percent beginning in 2014 because of apportionment recalibrations.

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San Francisco, Calif.



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At the city level, San Francisco offers several resources, such as rehabilitation funding, construction funding and long-term debt financing. The Mayor's Office of Housing and Community Development said the city's voter-approved Housing Trust Fund will increase from \$20 million annually to reach more than \$50 million annually and will be used for the acquisition, rehabilitation, preservation and new construction of affordable housing, as well as down-payment assistance and housing stabilization programs. City officials said they are considering dedicating the annual growth in the fund to rehabilitating the city's public housing stock.

San Francisco also has an inclusionary affordable housing program, which requires residential developments with 10 or more units to provide 12 percent of on-site units or 20 percent of off-site units as affordable to low- or moderate-income households. Alternatively, developers can pay a fee to the city's affordable housing program. At press time,

the mayor's office said that 83 percent of developers set aside affordable units on-site, 3 percent develop off-site and 14 percent pay the fee.

Looking Ahead

San Francisco housing experts predict continued demand for affordable, multifamily rental housing, but expect rents to plateau as more units come online. Overall, they agree that the city's affordable housing supply has a long way to go before it even comes close to the ever-increasing demand, but they remain optimistic. Schnur said, "We're hopeful that, with market rate projects beginning to throw off impact fees and the housing fund approved, there should be more funds [for affordable housing] in the next few years." ❖

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This article first appeared in the January 2014 issue of the Novogradac Journal of Tax Credits.

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