

## HIGHLIGHTS

### The Market Slowdown and Home Prices in the Suburbs and “Exurbs”

When faced with high home prices in America’s largest cities, many potential homebuyers seek affordable housing options in the suburbs. Prices in the suburbs are generally lower for homes of similar quality and, as the distance to the center city increases, prices often fall. In some cases, lower-income buyers seek homes in particularly distant suburbs, sometimes described as the “exurbs,” to find home prices that match their budgets.

In the latest housing boom, as the affordability concerns increased in many cities across the U.S., many homebuyers sought houses in increasingly distant suburbs. While it has been widely reported that sales and building activity was significant in such communities during the boom, an important empirical question is: “How robust was suburban price appreciation *relative to price appreciation in the inner city and close-in suburbs?*” If appreciation in the distant suburbs was as great as it was in close-in communities, then the housing boom had a particularly intense impact on affordability because it closed off places new homeowners could traditionally look for reasonable housing solutions. This article analyzes relative suburban and urban price appreciation during the housing boom for the eight most populated U.S. metropolitan areas: New York, Los Angeles, Chicago, Philadelphia, Dallas, Miami, Washington, D.C., and Houston. It also studies relative price trends since the housing market deceleration began a year ago. If increases in home inventories have been particularly dramatic in the most distant communities, as some have suggested, then home price data should reveal relative price weakness in the suburbs and exurbs.

The empirical findings suggest that, during the first five years of this decade, appreciation rates were quite similar for close-in and more distant homes. During that period, suburban and exurban appreciation closely resembled urban appreciation in each of the eight metropolitan areas studied. In the latest year, the same uniformity does not exist. In five of the eight markets, the recent deceleration has had similar effects in urban and suburban communities, but urban and suburban price trends have diverged sharply in New York, Los Angeles, and Miami. Although the cause of the different trends in the latter group of cities is not entirely clear, it may be related to the absence of affordable housing in the suburbs.

To begin analyzing price trends in urban and outlying areas, five separate repeat-transactions house price indexes are computed for each of the eight most populous metropolitan areas.<sup>1</sup> A “city center” index is computed for homes within 10 miles of the city center, and four additional indexes are produced for homes of similar distances to the city center. Distances are computed based on house zip codes and city latitude and longitude coordinates provided by the U.S. Geological Survey (USGS). The city center coordinates are for the largest city within the metropolitan area (e.g., center city Chicago is used as the “center” of the Chicago-Naperville-Joliet Metropolitan Statistical Area).<sup>2</sup>

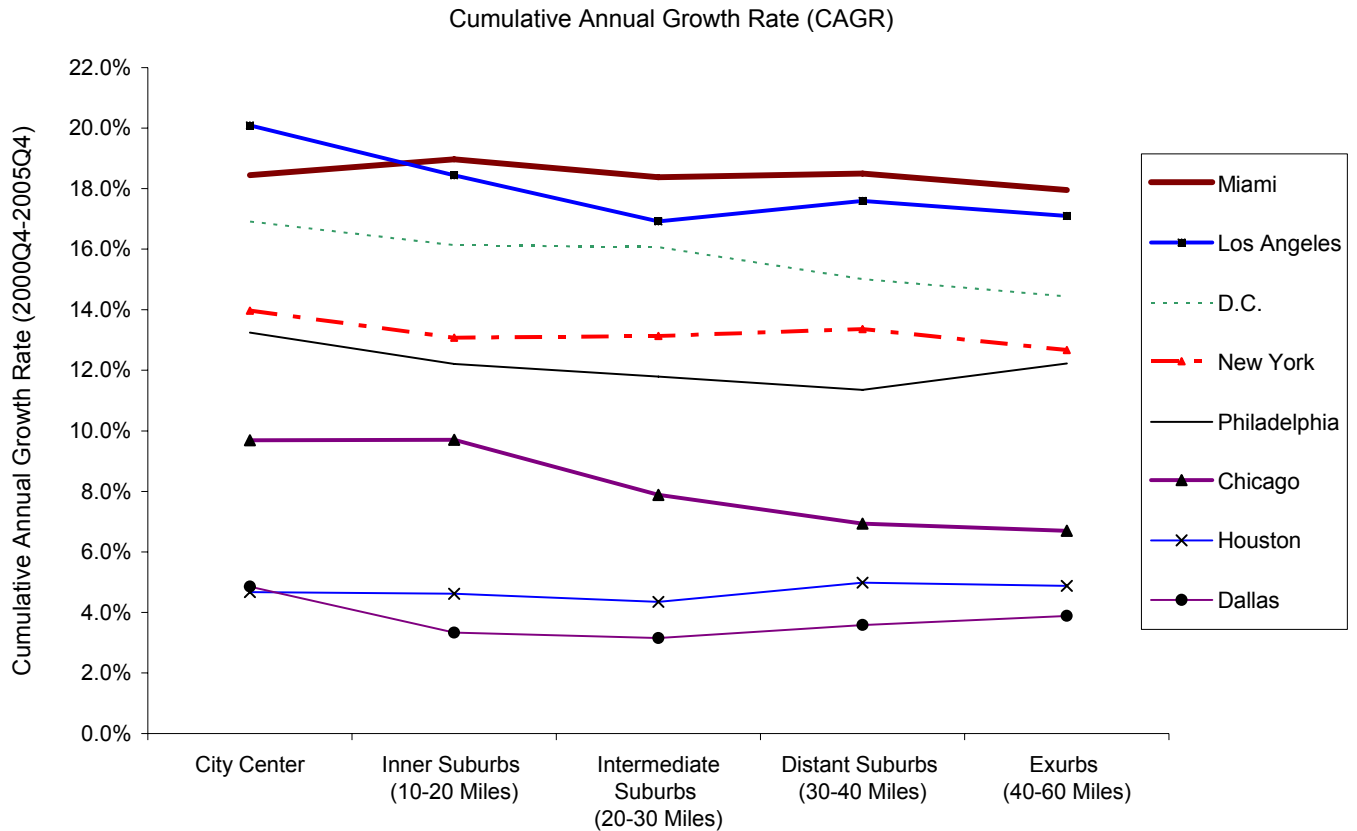
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<sup>1</sup> The indexing methodology used here is identical to that used in the construction of OFHEO’s basic house price index.

<sup>2</sup> These groupings are not official government-defined categories. Moreover, the USGS assigns city center coordinates using early landmarks such as city halls and these may differ from the actual business or population center.

Houses are grouped into the following distance intervals: 10-20 Miles (“Inner Suburbs”), 20-30 Miles (“Intermediate Suburbs”), 30-40 Miles (“Distant Suburbs”), and 40-60 Miles (“Exurbs”).

**Figure 1: Suburban Price Appreciation During Strongest Period (2000Q4-2005Q4):**

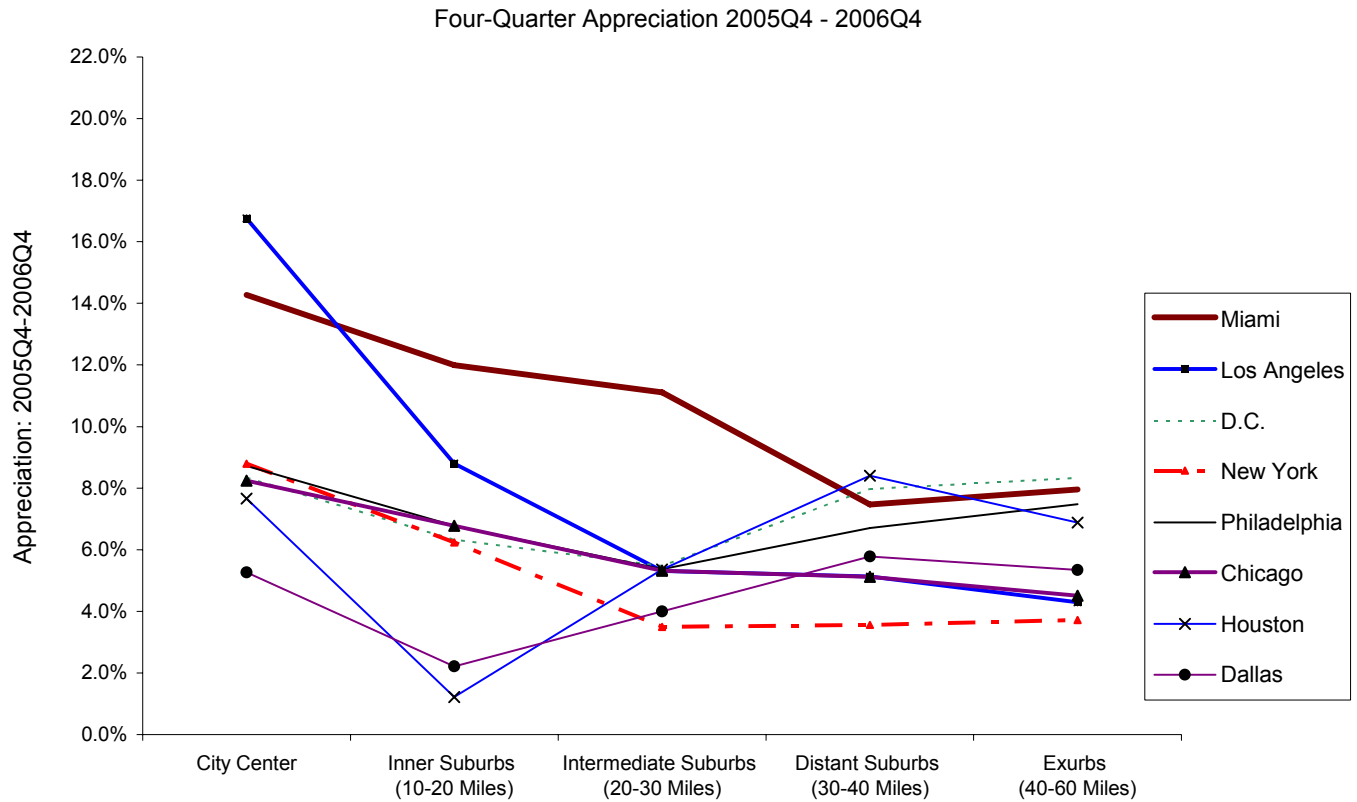


For the eight large metropolitan areas, Figure 1 reports average annual appreciation rates for the early part of the decade: the fourth quarter of 2000 through the fourth quarter of 2005. Each line represents appreciation for different parts of the same city, with appreciation in the urban core shown on the left and growth rates for increasingly distant suburbs shown at the right. Average annual appreciation in the Chicago city center was about 10 percent, for example, and declined for more distant suburbs. Average annual appreciation was about 7 percent for the most distant suburbs and exurbs.

The most striking feature of Figure 1 is the extremely close relationship between appreciation in the various distance intervals. Although appreciation rates were generally lower for more distant suburbs, the difference between price growth in the city center and outlying areas was minimal in almost every city. In Washington, D.C. and Los Angeles, where appreciation in the close-in areas averaged between 17 and 20 percent per year, price growth in the distant suburbs and exurbs trailed urban rates by only about 3 percentage points. The difference in appreciation rates was negligible for New York and Miami. In Dallas and Houston, where the effects of the housing boom were generally limited, appreciation rates were almost identical for the different distance intervals.

Figure 1 suggests that the effects of the housing boom (whether large or small) were spread relatively evenly in close-in and farther out communities. Figure 2, which shows price changes over the latest year, is not so clear. The relative impact of the slowdown has been particularly intense in exurban communities in some metropolitan areas, while the effects have been relatively symmetric in other cities.

**Figure 2: Suburban Price Appreciation in Latest Year**



The widely-reported market weakness in the distant suburbs is evident, at least in relative terms, in New York, Los Angeles, and Miami. Home price appreciation slipped but remained at historically high levels in those city-centers, but appreciation in the distant suburbs and exurbs fell sharply in all three cities. For instance, in New York and Los Angeles, price appreciation in the exurbs was four percent, far below the 17 and 9 percent rates in the city centers. In Miami, appreciation rates in the distant suburbs and exurbs were more than 6 percentage points below the city-center rate.

The relative rates of deceleration were generally quite similar for other cities. As was the case during the prior five years, appreciation rates were nearly identical in the latest year in suburban and urban Washington, D.C. In Chicago and Philadelphia, recent appreciation rates in the exurbs lagged price growth in the city center by about 2-3 percentage points: a difference very much in line with what was seen in prior years. In Dallas and Houston, price appreciation has remained at a relatively steady pace for homes in all distance intervals.

With the relative weakness only evident in select cities, the question becomes: “What makes the New York, Los Angeles and Miami markets different?” Price dynamics in housing markets are affected by a complex mix of demand and supply factors, many of which are unique to local economies. Table 1 nevertheless identifies a commonality among the three cities with relative weakness in exurb markets.

**Table 1: Affordability, Suburban Prices, and Recent Price Trends**

	City-Center Appreciation 2005Q4-2006Q4	Exurb Appreciation 2005Q4-2006Q4	Relative Home Expense (Price/Income Ratio)	Price Ratio (Average Price in Exurbs / Average Price in Center City)
<b>New York</b>	<b>9%</b>	<b>4%</b>	<b>7.2</b>	<b>94%</b>
<b>Los Angeles</b>	<b>17%</b>	<b>4%</b>	<b>11.4</b>	<b>173%</b>
Chicago	8%	5%	4.5	90%
Philadelphia	9%	7%	4.1	128%
Dallas	5%	5%	2.7	74%
<b>Miami</b>	<b>14%</b>	<b>8%</b>	<b>7.6</b>	<b>98%</b>
Washington, D.C.	8%	8%	5.6	74%
Houston	8%	7%	2.9	79%

In those three cities, house prices are very high and prices in the distant suburbs do not offer any affordability relief. The third and fourth columns in the table provide the relevant statistics. The third column, “Relative Home Expense,” reports the ratio of median home prices to median incomes for the metro area.<sup>3</sup> The fourth shows relative prices for the exurban homes, where prices are reported as a percentage of average home prices in the city center. For instance, a figure of 75 percent would suggest that exurb homes are, on average, 25 percent less expensive than houses in the city center.<sup>4</sup>

The table reveals that the three least affordable housing markets (as measured with the price-to-income ratios) are New York, Los Angeles and Miami—the cities with the relatively weak exurb markets. In all of these areas, home prices in the exurbs are generally close to if not

<sup>3</sup> These data were obtained from the “2007 Demographia International Housing Affordability Survey” available at: <http://www.demographia.com/dhi-ix2005q3.pdf>.

<sup>4</sup> Note that home quality is not controlled for in these comparisons. Differences in home attributes may explain some of the divergence in average prices.

above prices in the center city. In New York and Miami, prices are only 4 to 8 percent lower in the exurbs and, in Los Angeles, prices are actually 73 percent higher for distant homes.

For the other large cities—those that have not experienced the same market asymmetry in the latest year—affordability issues are either less severe or home prices in the exurbs are attractively priced. In the Washington, D.C. area, for example, the price-to-income ratio is a relatively high 5.6, but distant homes are 26 percent less expensive than they are in close-in areas. Conversely, homes in the Philadelphia exurbs are more expensive than their downtown counterparts, but home prices are a much lower multiple of incomes.

While the different trend in New York, Miami, and Los Angeles is interesting, caution must be exercised in interpreting the result. To the extent that the recent housing market deceleration is affecting homes in various price tiers differently, the results in Table 1 in part may be reflecting those differences. A more complete analysis would compare price trends in suburbia to trends in city centers *for similarly priced homes*. Unfortunately, sufficient data are not yet available to facilitate such an exercise. Given that the housing market slowdown has been underway for only about a year and a half, considering the relatively small size of the geographic areas under review, several quarters may need to pass before such empirical work can be performed with reasonable precision.