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Recession Remedies Podcast

“What economic policies prevented dire housing outcomes during COVID-19?”
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Guests:

LAURIE S. GOODMAN
Vice President, Housing Finance Policy
Urban Institute

PAUL WILLEN
Senior Economist and Policy Advisor, Research
Federal Reserve Bank of Boston

Host:

DAVID WESSEL
Director, The Hutchins Center on Fiscal and Monetary Policy
Senior Fellow, Economic Studies
The Brookings Institution

Episode Summary:

The COVID-19 economic policy response helped prevent dire outcomes for renters and homeowners with mortgages during the pandemic. How did the stars align to make forbearance an especially effective policy? What did the pandemic reveal about gaps in the rental assistance safety net? To discuss these questions and more on housing policy during COVID-19, host David Wessel is joined by Laurie S. Goodman, vice president of housing finance policy at the Urban Institute, and Paul Willen, senior economist and policy advisor for research at the Federal Reserve Bank of Boston.

WESSEL: Welcome to the Recession Remedies podcast, exploring lessons learned from the economic policy response to the COVID 19 pandemic, lessons that we should remember when the next recession hits. I'm David Wessel.

The pandemic posed an economic threat to many of the nation's 44 million renters and 79 million homeowners with mortgages, and the government responded with a variety of policies, including bans on evictions, deferral of mortgage payments, and more. Did they work as intended? Were they necessary given all the other federal aid provided? Should we repeat them? Laurie Goodman from the Urban Institute and Paul Willen from the Federal Reserve Bank of Boston are among the authors of a chapter that speaks to those questions in our "Recession Remedies" book, a joint venture of The Hamilton Project and the Hutchins Center at Brookings. You can read the whole book online for free at Brookings dot edu slash Recession Remedies.

So, Laurie and Paul, thanks for joining us today. Let's start with a snapshot of where we were in the housing market going into the pandemic at the beginning of 2020. Paul, can you talk a little bit about what was the situation for homeowners, particularly compared to what we saw in the Great Recession of 2007, '08, and '09?

WILLEN: So, I'm speaking today as a researcher and a concerned citizen and not as a representative of the Federal Reserve Bank of Boston or of the Federal Reserve System.

I think the housing market was in was it was quite healthy in 2019. There had been a fair amount of price growth, which in the past had been a cause for concern, so house prices where were growing, you know, in the 4, 5, 6% range in the years preceding the pandemic.

But it was healthy in the sense that it mostly reflected fundamentals, it reflected, for the most part, increases in in rent. So, in other words, it reflected the fact that people wanted to consume housing as a good or as a service rather than as a speculative tool, which is what had happened in the 2000s.

So, in that sense, things were good. Interest rates had come up. So, the period of unusually low interest rates that we had earlier in the decade, interest rates had returned to more normal levels and yet house price growth remained healthy. And affordability did not appear to be a big problem. Interest rates were coming down before the pandemic, so we were already seeing some increase in refinance activity. But for the most part, I think the housing market was quite healthy heading in.

WESSEL: Right. I guess the most significant thing that struck me is that there were many fewer people who had negative equity in their homes going into the pandemic then as we went into the Great Recession.

WILLEN: For all practical purposes, it was as low as it's going to get. House prices turned the corner in 2011, 2012. So, even the people who had bought in 2004, 2005, 2006, even those people were probably okay between amortization and house price appreciation, they were okay. And obviously anybody who bought starting in 2010, say, had a big equity cushion.

WESSEL: Great. So, Laurie, what was the circumstance with renters going into the pandemic? And in general, how are renters different economically from homeowners?

GOODMAN: Thank you very much for the question and thanks for having me on today. Renters are generally much less affluent than homeowners. The median income of renters in 2019 was about 42,000. It was about 81,000 for homeowners, 96,000 for those with a mortgage, and about 58,000 for those without. So, renters have much lower incomes, they also have much, much lower wealth. The median wealth for a renter in 2019 was about $6,300. The median wealth for a homeowner in 2019 was about $255,000. So, remember, renters much less affluent than homeowners.

And then the other thing to realize is that three out of every four renters that actually qualifies for federal housing assistance does not receive it. There's just simply not enough money to go around to provide rental assistance for everyone that qualifies for it.

WESSEL: So, going into the pandemic, which people were most cost burdened, that is which people had to spend more than 30% of their income on rent?

GOODMAN: Yes, so going into the COVID pandemic, what you found is that a lot of renters spent more than 30% of their income on rent. Close to half of all renters spend over 30% of their income on rent and close to a quarter spend more than 50% on rent. If you break that down by income buckets, what you find is that over 80% of those under 25,000 a year are cost burdened. That is, they spend more than 30% of their income on rent. The numbers go down sharply for higher income levels.

WESSEL: Right. So, basically, homeowners were in pretty good shape, even those with mortgages, going into the pandemic. And renters, as is often the case, we're not in great shape and they were somewhat more vulnerable to the shock of losing a job or losing hours or something like that. So, Paul, I wonder if you could identify the two or three most important things that the government did for homeowners in response to the pandemic.

WILLEN: Well, for home owners, the first thing the government did that had a big effect was forbearance. And so the CARES Act required that lenders more or less automatically allow borrowers basically to miss payments without any without any penalties. So, normally when you miss a payment, a mortgage payment, you're reported to the credit bureau. I mean, a lot of bad things happen. You pay fees and you're required to become current again. To become in good standing with the lender you're required to repay all the missed payments.

And so what the what the CARES Act did was basically allow borrowers, all they had to do was to attest to some hardship from COVID. There was no documentation requirement. And they were then they could initially up to six months of payments, and then later it was extended to 12 and then to 18. And that happened more or less immediately. And so even the timing was good. The CARES Act was passed in in at the end of March. Mortgage payments for borrowers are typically not late until the 15th of the following month. And so that meant basically borrowers could skip their April payment, the payment that was due right away, without any penalty.

And so that program was excellent in the sense that it provided relief to borrowers right away. There was no delay. If we contrast that with the programs in 2009 and 2010 where it took forever for the government to roll the programs out, and then even when they did, borrowers had an enormous bureaucratic burden to get any relief.

WESSEL: So, the fear is always what economists call moral hazard, that people will take advantage of this even though they didn't need it. What do you think about that in this regard?

WILLEN: You use one piece of jargon, which is a "moral hazard," and I'll put back another, which is this phrase "incentive compatible." What's good about forbearance is that the borrower is expected to eventually repay the missed payments. So, the way it typically worked for forbearance is that either some borrowers were just able to repay all the missed payments. But if they couldn't, the lender would put a second lien on the property covering all the missed payments, a non-interest bearing second lien. And that was due when the borrower either refinanced or sold the property.

But the point is the borrower did have to eventually pay the money back. And that meant that the incentive for someone to get forbearance who didn't need it was limited. And then in that sense, if we contrast that with the modifications in 2009 and 2010, in those cases borrowers were getting relief that they did not have to pay back. And for that reason, lenders really needed to make sure the borrower needed the assistance because otherwise they would be giving, as you describe, the assistance to people who just wanted assistance but didn't actually need it.

WESSEL: I see. Okay, so what would be your next on your list?

WILLEN: So, there were two policies which were not precisely aimed at the housing market, at homeowners, but which were aimed at helping homeowners. Well one in a sense was aimed at homeowners and didn't work, and one wasn't particularly aimed at homeowners, but did. So the one that I think did not work as well as it could have was reductions in interest rates. So, homeowners obviously have mortgages and they pay interest on mortgages. And so you might think that when the Federal Reserve cut interest rates to zero and particularly when we bought mortgages to drive down the rate on mortgages, that that would have benefited homeowners. And it did.

But the benefits were both much smaller than the costs and it took a long, long time to improve household balance sheets. So, one thing which I've documented in other work is that in order to get those reductions in interest rates, borrowers needed to refinance. And at the time, there was very limited capacity in the industry. And the result was that a lot of the benefit of refinancing actually ended up accruing to the mortgage companies, which handled the transactions rather than to the borrowers.

WESSEL: You also looked at how did this affect Black and Hispanic borrowers different from white borrowers? And I wonder if you could just talk about what you found there.

WILLEN: So, we found a pattern that we've seen in the past, which is that that white borrowers were much more likely to take advantage of the opportunity to refinance than Black or Hispanic borrowers. And the kind of overall number is that of the payment savings that borrowers got from reduced interest rates, Black borrowers got between 3 and 4% of the benefit of that, and they account for 8% of homeowners and 15% of the population. So, the benefits of these programs disproportionately went to white and to an extent to Asian homeowners. And that's even when we control for observable differences, the fact that Black homeowners have lower income and different credit profiles. Even when we control for those things, we still see those differences.

WESSEL: And the next one, the one that did work?

WILLEN: Oh, the one that did work was, then Laurie will also mention this, was the unemployment insurance. So, the CARES Act, this expanded unemployment insurance, gave $600 a week. And I remember when we heard about that, this was in the end of March, the stress level that we felt about households and making their mortgage payments went down a lot because we knew that millions, tens of millions of people were losing their jobs. And we expected that many of those people would be unable to make their mortgage payments.

And then, when we found out that the CARES Act had given people $600 a week, which you multiply that by four, that's $2,400 a month, we thought, well, that will make a big difference. And I think it did. I think the numbers we had expected for forbearance when we were first discussing this in March, the numbers that we actually saw came in way, way lower than we had feared. And I think a large part of that was the expanded UI.

WESSEL: Interesting. So, Laurie, let me ask you the same question. What were the couple of things that the government did for renters that had the most oomph?

GOODMAN: So, basically there were three policy interventions that were quite important. There was the expansion in the unemployment benefits, which Paul talked about. There was also eviction moratoriums and emergency rental assistance.

I think the expanded unemployment insurance was very, very helpful for those who had a job and were laid off from their job. And it actually contained the effect of the pandemic on the rental community. So, if you had a job and you qualified for the enhanced unemployment insurance, you were initially better off because in many cases because of the extra $600 a week.

If you look at the percent of households that were behind on rent payments, you found that it remained pretty steady throughout the pandemic. It came down a little bit, but it was actually pretty steady, whereas unemployment went way up and then came way down.

So, the disconnect is that a lot of households, particularly lower income households, were cost burdened going into the pandemic. You had many households that didn't qualify for the enhanced unemployment insurance either because they lost hours but didn't lose enough hours to qualify, or didn't qualify because of citizenship status or whatever. And many of those households had problems paying their rent throughout.

The eviction moratoriums were incredibly important early on. Estimates are that evictions were about 50% lower than they would have been in the absence of the eviction moratoriums. So, if you were having trouble paying your rent, the fact that you couldn't get evicted basically reduced deaths due to COVID. It provided a safety net that allowed households to redirect the funding to food, to other necessities. It cut down on mental stress, and it prevented homelessness. Remember, we have a lot of families who were doubled up and the eviction would have affected more than one family. So, certainly that was that was very, very important early on.

The problem with eviction moratoriums is that they're not a long-run solution. The tenant still owes the money and the landlord still has to pay to maintain the property. The long-run solution should be should have been emergency rental assistance. There was an emergency rental assistance program that was put into effect, but it was very, very slow to roll out. It was put into effect at the end of 2020, the first slug of it, but it took a long time for that to roll out.

Now, it's important to realize that to qualify for emergency rental assistance, you had to have an income less than 80% of area median income. So, those that qualified in many cases were those that were cost burdened before the pandemic, may have lost some hours, had a pandemic shock, and hence remained severely cost burdened.

But the slow rollout of the program put a lot more pressure on the eviction moratorium than it otherwise might have. And I think part of the reason the roll out of the program was so slow is that they were pushing it out through state and local channels. And many of these state and local governments didn't have a system in place to distribute the money, so they basically had to stand up brand new programs.

WILLEN: I just wanted to add one thing. I remember early on in the pandemic, there was some data that came out that initially shocked us that something like 20% of people were late on their rent payments. But then we looked into it and it turned out that apparently 20% of people are always late on their rent payments. And so, I think it kind of highlighted the difference between the mortgage market where people make their mortgage payments, people in the rental market are always more vulnerable and had been more vulnerable before the pandemic.

GOODMAN: And I think, Paul, to that, I think that's a very good point. But I do want to point out that, yes, the percentage of people that were behind on their rent payments did go up. We can argue about how much it went up. Certainly, the quality of our data on the rental side is much lower than the quality of data on the mortgage side. So we really don't know how many people were late on their rental payments prior to the pandemic. The last time that information was collected was actually 2017. And so we were comparing pandemic numbers to the 2017 American Housing Survey numbers.

In addition, survey data can oftentimes be different than administrative data. The survey data covered a wider swath of the population, but the survey data showed a higher percentage behind than the limited administrative data that we had covering various segments of the market.

WESSEL: So, both of you mentioned the importance of expanded unemployment insurance benefits, which makes sense given that the people most vulnerable are the people who lose their jobs. We also had substantial stimulus checks, the Economic Impact Payments, including the 1,400 dollars per person slug in March 2021. If we did enough with income support, if we gave people, particularly vulnerable people, enough money so they could pay their rent or make their mortgage payments, do we need to do all these other housing-specific things?

WILLEN: It's a good question. Let me say that the income support programs was a patchwork. It was also the PPP. And so, putting forbearance in place as well. And in a sense, we know a lot of people used forbearance despite all those programs. So, I think forbearance at least was still necessary. Would it alone have worked without the income support programs, it's harder for us to say. But I think those programs at least were useful in the sense that they covered all the other situations that the PPP and UI didn't cover.

WESSEL: I see. And what do you think, Laurie?

GOODMAN: I think that the enhanced unemployment benefits plus the economic impact payments were absolutely critical for those who lost their job as a result of the pandemic. And it made that part of the population relatively whole, allowed them to continue making their rental payments. It did a lot less for those that either didn't have a job or on the edge and lost a few hours. And that was the part of the population that was cost burdened before. And if you don't have a job, you don't qualify for the enhanced unemployment benefits. And a lot of those in less than 25,000 income range do not have a job or many family and family members are unemployed.

There's a big difference between the way the forbearance was rolled out to homeowners and the way the emergency rental assistance was rolled out to renters. In the case of the forbearance, it was automatic. You just told your servicer you needed forbearance, you attested to the fact that you had had a COVID hardship, and it was done.

The emergency rental assistance was done in a very, very decentralized manner. Every state and local government had their own set of documentation requirements. Some of these documentation requirements were onerous. The rental community is on average, much less affluent. In many cases, public libraries were the heroes because they were helping tenants upload information to send in. So, it was a far more documentation-intensive process, which just took an order of magnitude longer to roll out and therefore made it at the end much, much less effective.

WESSEL: So, Laurie, do you think that we're better positioned now that we've done this? After all, I remember talking to some people at the Treasury and they said, We've never done this thing where we have to reach out to landlords and tenants through state and local governments. But now they have an apparatus and some experience. Do you think if we needed to do this again, we'd be better? Or is it just conceptually just too complicated to do this through state and local governments?

GOODMAN: I think it can be done as long as the programs remain standing. But I think once the funding runs out the programs disappear. And next time you're going to be in the same boat standing up new programs from scratch.

WILLEN: Just to add, I mean, this brings in something that has already come up. But I mean, the mortgage industry is big companies, even a small mortgage servicer has thousands, tens of thousands of loans. And as a result of that, we have great data. We can go to these large organizations which have the resources to compile tons of data. So we have mountains of information about homeowners with mortgages.

With renters, I mean, Laurie can correct me on this, but I mean, it's still a huge fraction of landlords are mom and pop operations.

GOODMAN: Yes.

WILLEN: And then to make it even harder in this situation, this wasn't borrowers making payments to investors in mortgage backed securities. This was borrowers making payments to landlords who depend on that income to live. And so the problems were just of a scale and a complexity that was something that, the mortgage problem was in some sense easy.

WESSEL: Sure. So I'm afraid that the next recession is going to arrive sooner than I anticipated when we started this project. I'm curious if you were called to a congressional hearing and asked, Well, we're having another recession, it has nothing to do with the pandemic, what that we did during COVID-19 should we repeat? What should we avoid or what should we do differently? Laurie, do you want to start?

GOODMAN: Sure. So, what you really want to do first is expand federal rental support so a greater proportion of those people who qualify for federal for federal housing assistance receive it so that the next shock is less devastating to the rental community. I mean, basically, the crisis highlighted the need for a more permanent rental assistance safety net so that when you finally get the shock, fewer people are affected.

I think the income replacement was extremely valuable. We certainly want to do that again. It basically cushioned people who were directly affected by the shock.

The eviction moratorium was necessary in this case. I am not sure that in the next recession you'd necessarily want to do that. It depends on the extent of the rental assistance you have in place. The reason you might not necessarily want to do that is because if there's no health risk involved and you've got adequate rental assistance, again, the landlord needs that money to maintain the property and to live on. So, you want to be a little bit cautious about using eviction moratoriums going forward. But certainly the cash payments and the emergency rental assistance are musts.

WESSEL: Paul, what would you tell them?

WILLEN: So, one thing I would say is that the use of forbearance, I don't think it's a cure all, but I do think that there are many borrowers who would benefit from it, that in a way it allows borrowers to tap into their home equity in a very low-burdened way. I mean, they can basically take a loan against their home and show up in the form of the second lien if they can't pay the loan back.

And in fact, I think Fannie Mae and Freddie Mac are ahead of Congress. There's a sense already that putting forbearance into the loss mitigation, as they call it, toolkit is something, it's a resource that we can definitely use in ways that we didn't really imagine before the pandemic.

The only other thing I would say for Congress, and the problem is this is not something we can do kind of in an emergency way, but is to find ways to make the process of refinancing and taking advantage of low interest rates less burdensome than it is. And one of the things that's puzzling about the process right now is that the industry treats every refinance as if the borrower has never had a mortgage, as if the financial system is not already exposed to the risk. And so, I think from a financial stability standpoint, allowing borrowers to refinance more easily actually will reduce the risk to the financial system. So, finding ways to allow borrowers to take advantage of that is something that we need to do probably before we have the next recession. It's not something we can implement overnight.

WESSEL: Right. Well, I think both of you have pointed out that the pandemic exposed some preexisting conditions. Paul, you mentioned the strange system we have for refinancing mortgages, which of course is an aftereffect of having a 30-year fixed-rate mortgage in the first place. And Laurie, you've pointed out that we had problems in the rental market before, that people who were eligible for federal assistance don't get it because there's not enough money. And we should fix that before the next recession as well.

I want to thank both of you for both the hard work you did on this chapter and for joining us today. I think that we learned a lot during the pandemic, and our effort here is to make sure we don't forget it before the next recession arrives. As I said earlier, you can read this chapter and the whole book online for free at www dot Brookings dot edu slash recession remedies.

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