Memorandum

DATE: December 18, 2018

TO: PN Hoffman

FROM: Leonard Bogorad, Managing Director, RCLCO

SUBJECT: Analysis of Potential Impact of the Waterfront Station II Development on Destabilization of Property Values, Displacement, and Gentrification

RCLCO (Robert Charles Lesser & Co.) was retained by PN Hoffman (the "Applicant") to evaluate whether the Waterfront Station II development at 1000 Fourth Street, S.W., will cause destabilization of land values, displacement of neighborhood residents, and gentrification in the surrounding neighborhoods.

Waterfront Station II is proposed to include approximately:

- 450 rental apartments, including 30% affordable units
- 9,000 square feet of educational/daycare space
- 11,000 square feet of retail
- 9,000 square feet of arts/cultural space

RCLCO has extensive experience conducting fiscal and economic impact analyses for public and private sector clients, and has worked on such projects as DC USA, developments in the NoMa area and the area near the ballpark, Downtown Silver Spring, and National Harbor.

Overall Conclusions

- New housing in all price ranges helps to mitigate increasing prices and rents. Locally, the amount of apartment construction at a District-wide level has had a measurable impact on rent growth. Waterfront Station II will add 450 new housing units. In addition, 30% of the units in the development will be affordable, with very deep subsidies.

- Waterfront Station II will be developed on a vacant site and will not result in any direct displacement of neighborhood residents.

- The development will provide other benefits for neighborhood residents: educational/daycare space, retail, and arts/cultural space.

- The neighborhoods surrounding Waterfront Station II are already experiencing increases in property values and rents that will likely continue whether or not the development occurs. Waterfront Station II will not set home price, rent, and land value destabilization in motion; rather, these trends have long been occurring without any impetus from the development. There is no reason to conclude that Waterfront Station II will have a significant impact on this established trend of home price and rent increases.

- Despite the long-standing gentrification, the surrounding neighborhoods have a wide range of housing, including 493 public housing units at Greenleaf.

Overall, not only will Waterfront Station II not add in any significant way to the gentrification that has already been occurring in the surrounding neighborhoods, it will in fact help to mitigate negative impacts of gentrification and deliver many positive impacts. The project will provide a significant increase in the total number of housing units, which will help to correct the imbalance between housing demand and supply; dedicate 30% of the units to lower-income households; and provide educational, cultural, and retail benefits. These are exactly the types of benefits that are vital to offsetting the negative impacts of gentrification.

One of the Causes of Higher Housing Prices and Rents Is an Imbalance between Demand and Supply, so Development of New Housing Is Critical

Development of new housing is very important for the District. Waterfront Station II will add approximately 450 new housing units to the District and the Southwest/Waterfront neighborhood.

Academic studies and articles written from a wide range of political perspectives are increasingly finding that addition of new housing of all types and price ranges is one of the key steps that can be taken to mitigate rising housing prices and rents.

The Legislative Analyst's Office ("LAO") of the California Legislature has conducted extensive research and analysis on this topic, and concluded:

> As market-rate housing construction tends to slow the growth in prices and rents, it can make it easier for low-income households to afford their existing homes. This can help to lessen the displacement of low-income households. Our analysis of low-income neighborhoods in the Bay Area suggests a link between increased construction of market-rate housing and reduced displacement.[1]

The LAO explains the causes of this phenomenon as follows:

- Lack of supply drives high housing costs.
- Building new housing indirectly adds to the supply of housing at the lower end of the market in multiple ways.
- Housing generally becomes less desirable, and therefore less expensive, over time, with some middle-income households typically moving out of older housing, thereby making it available for lower-income households.
- But lack of new construction can slow this process.
- New housing construction eases competition between middle- and low-income households.
- More supply places downward pressure on prices and rents.

Richard Florida, a leading urban planner at the University of Toronto states that "We've long known … that restrictive land use and building codes in cities limit housing construction (and therefore housing supply), leading to increased costs, worse affordability problems, and deepened inequality in urban centers.[2]

And Jason Furman, the chairman of President Obama's White House Council of Economic Advisors, stated:

> Basic economic theory predicts—and many empirical studies confirm—that housing markets in which supply cannot keep up with demand will see housing prices rise.[3]

[1] Legislative Analyst's Office (2016). Perspectives on Helping Low-Income Californians Afford Housing.
[2] Florida, R. (2016). How Zoning Restrictions Make Segregation Worse. *The Atlantic Citylab*.
[3] Furman, J. (2015). Barriers to Shared Growth: The Case of Land Use Regulation and Economic Rents. Remarks to the Urban Institute.

Other economists making the same point range from Edward Glaeser of Harvard University writing for the Cato Online Forum[4] to liberal economist Paul Krugman. Krugman poses the question of why gentrification is happening so much in iconic U.S. cities, and one of his key answers is:

> Rising demand for urban living by the elite could be met largely by increasing supply. There's still room to build, even in New York, especially upward. Yet while there is something of a building boom in the city, it's far smaller than the soaring prices warrant, mainly because land use restrictions are in the way.[5]

John Mangin, writing in the Stanford Law and Policy Review, summarizes what he describes as "uncontroversial among urban economists":

> Underlying both of these phenomena—high housing costs in the suburbs and high housing costs in the cities—is a relatively straightforward problem of supply and demand. As demand to live in a particular suburb or city outstrips the existing housing stock, two things can happen: more housing gets built to meet the demand, or prices get bid up to ration the existing stock.[6]

As Matthew Yglesias explains in an article titled "Halting Construction Is a Terrible Way to Fight Gentrification":

> When you have enough construction, you get filtering rather than gentrification. Lower-income people move into dwellings that used to house rich people but that aren't shiny and new any more and don't have the most up-to-date fashions. When you don't have enough construction, you get rich people moving into poor people's houses and installing granite countertops.[7]

RCLCO's analysis found that the beneficial effects of new housing production on housing affordability can be seen in the District in the past few years. The amount of apartment construction at a District-wide level has had a measurable impact on rent growth. As the amount of new apartment construction increased, average annual rent growth trended down. In 2010 to 2012, a period during which only 718 rental apartments were delivered, rents grew between 2.3% and 6.0% annually. In the four years that followed, an additional 18,038 apartments were delivered, and rents only grew by 1.0% in 2016 and they declined by 0.4% in 2017. As all of the new buildings competed for leases, the market became more price-competitive. With a slower pace of deliveries in 2018, rents began to increase again (Exhibit 1).

The Applicant's Provision of Affordable Housing Will Be Particularly Valuable

Over and above the benefits of creating new housing at all price levels, development of new affordable housing helps to directly mitigate increasing rents and property values, decreases in affordable housing, and potential displacement of existing neighborhood residents.

The Applicant will be reserving an unusually high percentage—30%—of the approximately 450 units for affordable housing. Furthermore, these new, high-quality apartments will have very deep subsidies. Of the total units, 15% (68) will be reserved for households with incomes at or below 30% of the Area Median Income adjusted for household size, and another 15% (68) will be reserved for households with incomes at or below 50% of the Area Median Income adjusted for household size.

An Urban Institute study that involved case studies of six efforts to mitigate displacement in the face of gentrification found that production of affordable housing was "the key approach to addressing affordable housing needs in each of the six sites, regardless of the stage of the local housing market." The Urban Institute study also found that land availability was a significant issue, particularly in neighborhoods that

[4] Glaeser, E. (2014). Land Use Restrictions and Other Barriers to Growth. *Cato Online Forum*.
[5] Krugman, P. (2015). Inequality and the City. *New York Times*.
[6] Mangin, J. (2014). The New Exclusionary Zoning. *Stanford Law & Policy Review*.
[7] *Slate Moneybox*, April 4, 2013.

already had strengthening or strong housing markets. (As discussed below, the neighborhoods surrounding Waterfront Station II already have strong housing markets.) The report noted that one approach was for for-profit developers to include affordable units in their projects,[8] as will occur at Waterfront Station II.

Waterfront Station II Will Not Result in Any Direct Displacement of Neighborhood Residents

The Waterfront Station II site is currently undeveloped. This means that there are no residents living on the site, and there will be no displacement of residents of any income level as a result of the development.

Waterfront Station II Will Provide Other Benefits for Neighborhood Residents

Waterfront Station II will also include several ground-floor uses that will be beneficial to neighborhood residents:

- Approximately 9,000 square feet of educational/daycare space, currently contemplated as a pre-K/daycare facility for approximately 176 students.
- Approximately 11,000 square feet of retail, which will provide more retail options and job opportunities for area residents.
- Approximately 9,000 square feet of arts/cultural space, which will provide interactive cultural activities to the public.

The Surrounding Neighborhoods Have Already Been Experiencing Home Price and Rent Increases for Years, and Waterfront Station II Will Not Have a Significant Impact on this Established Trend

RCLCO's analysis determined that the neighborhoods surrounding Waterfront Station II have been experiencing home price and rent increases for years. Waterfront Station II will not set destabilized rents, home prices, and property values in motion. Rather, these trends have long been occurring without any impetus from Waterfront Station II. We have defined the relevant Southwest/Waterfront area as essentially the area of the District that is south of the Mall, west of South Capitol Street, and west of the Anacostia River—the Census Tract that includes the Waterfront Station II site, plus the three tracts that are close to the Waterfront II site. On some of the exhibits, we have shown separate data for each of the four Census Tracts that comprise the Southwest/Waterfront area (Exhibit 2).

- **Home prices in the Southwest/Waterfront Area have been increasing faster than in other neighborhoods.** Data from Neighborhood Info DC, a project of the Urban Institute (Exhibit 3),[9] shows that the median single-family home sale price, in constant dollars, for the area increased 31% between 2010 and 2016, as compared with 20% for the District overall. Whereas in 2010 the area's median sale price was $91,000 above the citywide median, the area's median price was $183,000 above the citywide median price in 2016 (all in 2016 dollars).

  As shown on Exhibit 4, median owner-occupied home values (as estimated by residents to the Census Bureau) in Census Tract 102 (within which Waterfront Station II is located) and Census Tract 64 increased much faster than in the District overall, based on a comparison between home values in 2006-2010 with values in 2012-2016. Exhibit 5 shows the substantial decrease in homes valued under $300,000, and the rapid increase in homes valued $500,000 and over, in the Southwest/Waterfront area between 2006-2010 and 2012-2016.

[8] Levy, D. et al. (2006). In the Face of Gentrification: Case Studies of Local Efforts to Mitigate Displacement, p. 77. Urban Institute: Washington, D.C.
[9] http://www.neighborhoodinfodc.org/index.html

- **Median rents in the surrounding neighborhoods are increasing.** The median rent in Census Tract 102 (within which Waterfront Station II is located) increased by 43% from 2006-2010 to 2012-2016, compared with 28% for the District as a whole (Exhibit 6). The median rent in Census Tract 110 increased by 59%. Rents in the other two Census Tracts comprising the Southwest/Waterfront area increased at approximately the same rate as the District as a whole, also a rapid rate. Exhibit 7 shows the striking change in the distribution of rents in the Southwest/Waterfront area between 2006-2010 and 2012-2016. Looked at another way, the absolute number of renter households with gross rents of under $1,000 in the area decreased by 49% from 2006-2010 to 2012-2016.

These findings regarding home price and rents increases in the neighborhoods surrounding Waterfront Station II make it clear that the development will not set destabilization of home prices, rents, or land value in motion; rather, gentrification has been a long-established trend without any impetus from the development.

This is consistent with a study that examined changes in the District's relative incomes, home values, and educational attainment by census tract to come to the same conclusion: that gentrification is already occurring in the area surrounding the Waterfront II site. This study by *Governing* magazine found that three Census Tracts in the Southwest/Waterfront area eligible to gentrify, and all three of these gentrified between 2000 and 2013 (see Exhibit 8 for map).[10] The study's methodology, as described in the footnote, was adapted from a widely cited gentrification paper by Columbia University professor Lance Freeman.[11]

Furthermore, with gentrification so far underway in the surrounding neighborhoods because of continuing growth, change, and housing demand relative to supply that have no relationship to Waterfront Station II, there is no reason to conclude that this development will have a significant impact on this established trend of home price and rent increases. A comprehensive 76-page review of the scholarly literature regarding gentrification and displacement discussed numerous causes of gentrification that were identified in many different studies, and none of these attributed gentrification to projects such as Waterfront Station II.[12] A study by Jeremy Jackson cited in the literature review observed no relationship between large-scale neighborhood investment projects and changes in nearby rents.[13] In any case, even if development of new market-rate housing could be a cause of gentrification—which ample evidence and analysis proves is not the case—the 315 new market-rate units planned for Waterfront Station II could not conceivably have such an effect.

Despite the Long-Standing Destabilization of Home Prices, Rents, and Land Values, the Surrounding Neighborhoods Have Housing that Serves a Wide Range of Income Levels

Although destabilization of home prices, rents, and land values are well-established trends in the surrounding neighborhoods, approximately one-fourth of the rental units have rents of less than $1,000. A notable component of the affordable units in the neighborhoods is the Greenleaf public housing development, which has 493 units. These units are expected to be replaced on a one-for-one basis as part of the redevelopment of Greenleaf into a mixed-income community.

[10] Study available here: http://www.governing.com/gov-data/washington-dc-gentrification-maps-demographic-data.html

[11] A census tract was determined to have gentrified according to three criteria: first, only the census tracts with a median household income and median home value in the bottom 40th percentile of the metro area at the beginning of the decade were "eligible" to gentrify. Gentrification was determined to have occurred if an eligible census tract's percentage increase in the inflation-adjusted median home value over the course of the decade was in the top third percentile for the metro area, and if the share of residents over age 25 holding a bachelor's degree at the end of the decade was also in the top third percentile.

[12] Zuk, M. et al. (2015). Gentrification, Displacement and the Role of Public Investment: A Literature Review.

[13] Zuk, p. 54; and Jackson, Jeremy (2008). Agent-Based Simulation of Urban Residential Dynamics: A Case Study of Gentrifying Areas in Boston. Thesis submitted to McGill University.

The Homeowners in the Surrounding Neighborhoods Benefit from Increasing Home Values

The homeowners in the neighborhood have benefitted from the increase in home values that has been occurring in the surrounding neighborhoods, and will likely continue with or without the Waterfront Station II development. Owners account for 40% of Southwest/Waterfront households.[14] Furthermore, the risk that neighborhood homeowners will be forced to sell involuntarily because of rising property taxes will be greatly mitigated by a range of District programs, including but not limited to:

- Homestead Deduction: For owner-occupant homeowners, deducts $72,450 from the property's assessed value when calculating the amount of property tax that must be paid.

- Senior Citizen or Disabled Property Owner Tax Relief: For homeowners 65 and over, or who are disabled, with total incomes of residents (other than tenants) of less than $128,950, the property tax is reduced by 50%.

- Tax Deferral for Low-Income Senior Property Owners:

    - For any homeowners with incomes of residents less than $50,000, any property taxes owed can be deferred with a 6% interest rate.

    - For seniors 75 and over with incomes of residents of less than $50,000 and interest and dividend income less than $12,500, who have lived in the District and owned a principal place of residence in the District for at least the past 25 years, any property taxes owed can be deferred with a 0% interest rate.

- Tax Deferral for Low-Income Property Owners: For any homeowners with incomes of residents less than $50,000, any property taxes owed can be deferred with a 6% interest rate.

- Assessment Cap Credit: Provides that a property may not be taxed on more than a 10% increase in the property's assessed value every year.

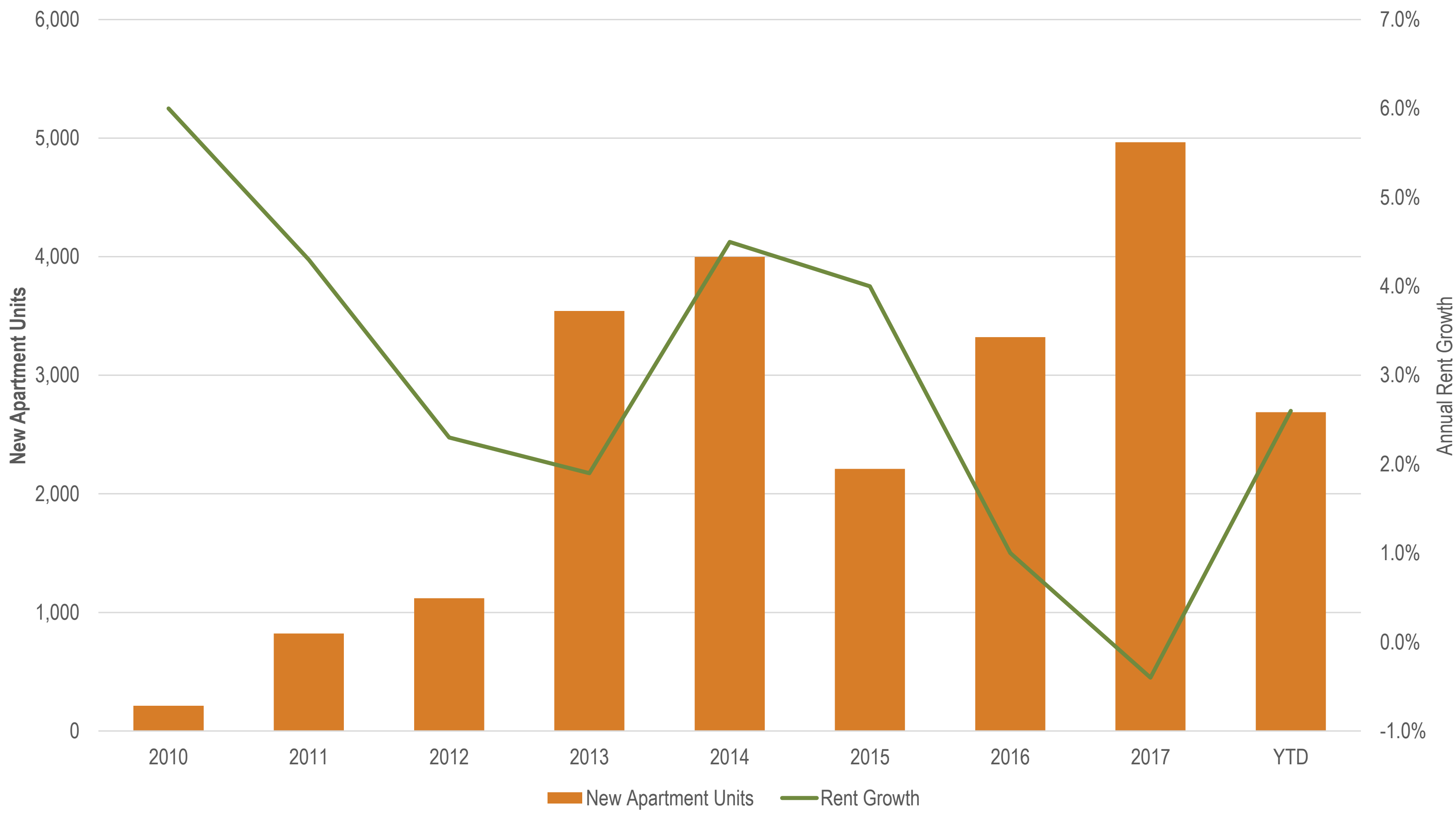
- Accessory Apartments: A recently adopted zoning provision allows owner-occupied homes to have an accessory apartment (Subtitle U § 201.1(d)), which was adopted to help homeowners stay in their homes even as property taxes and other housing costs increase.

[14] U.S. Census Bureau, American Community Survey, 2012-2016.

SUPPORTING EXHIBITS

Exhibit 1

Post-Recession Class-A Apartment Deliveries and Rent Growth
Washington, D.C.
2010-2018 YTD



Note: Rent growth is calculated net of any rent concessions.
SOURCE: CoStar

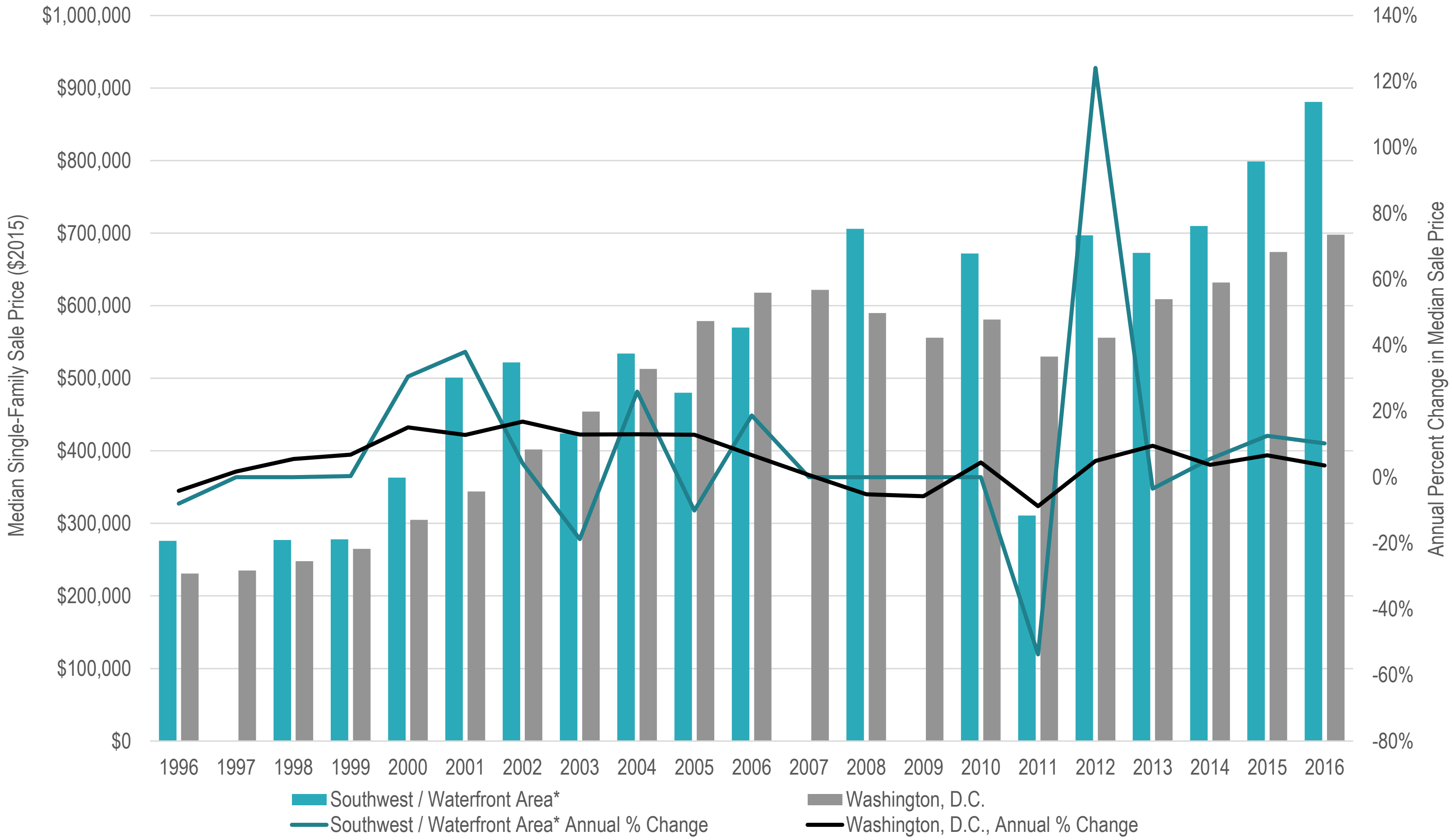
Exhibit 2

Southwest / Waterfront Census Tracts Map
Washington, D.C.
December 2018

SOURCE: ESRI

Exhibit 3

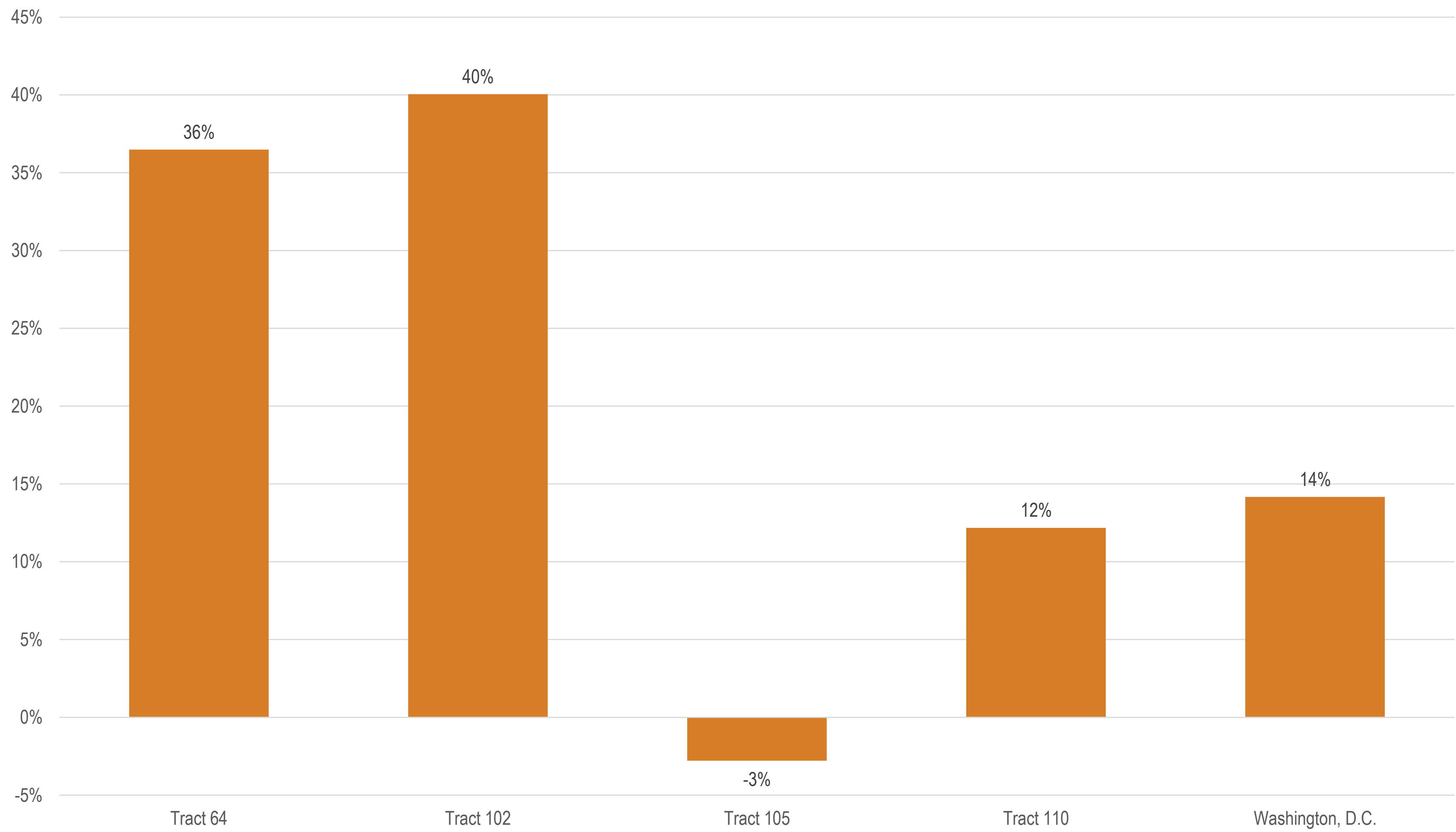
Median Single-Family Home Sale Price (2016 $)
Southwest / Waterfront Area and Washington, D.C.
1996-2016



** An area also referred to as "Neighborhood Cluster 22" in District government documents*
SOURCE: Neighborhood Info DC, a project of the Urban Institute

Exhibit 4

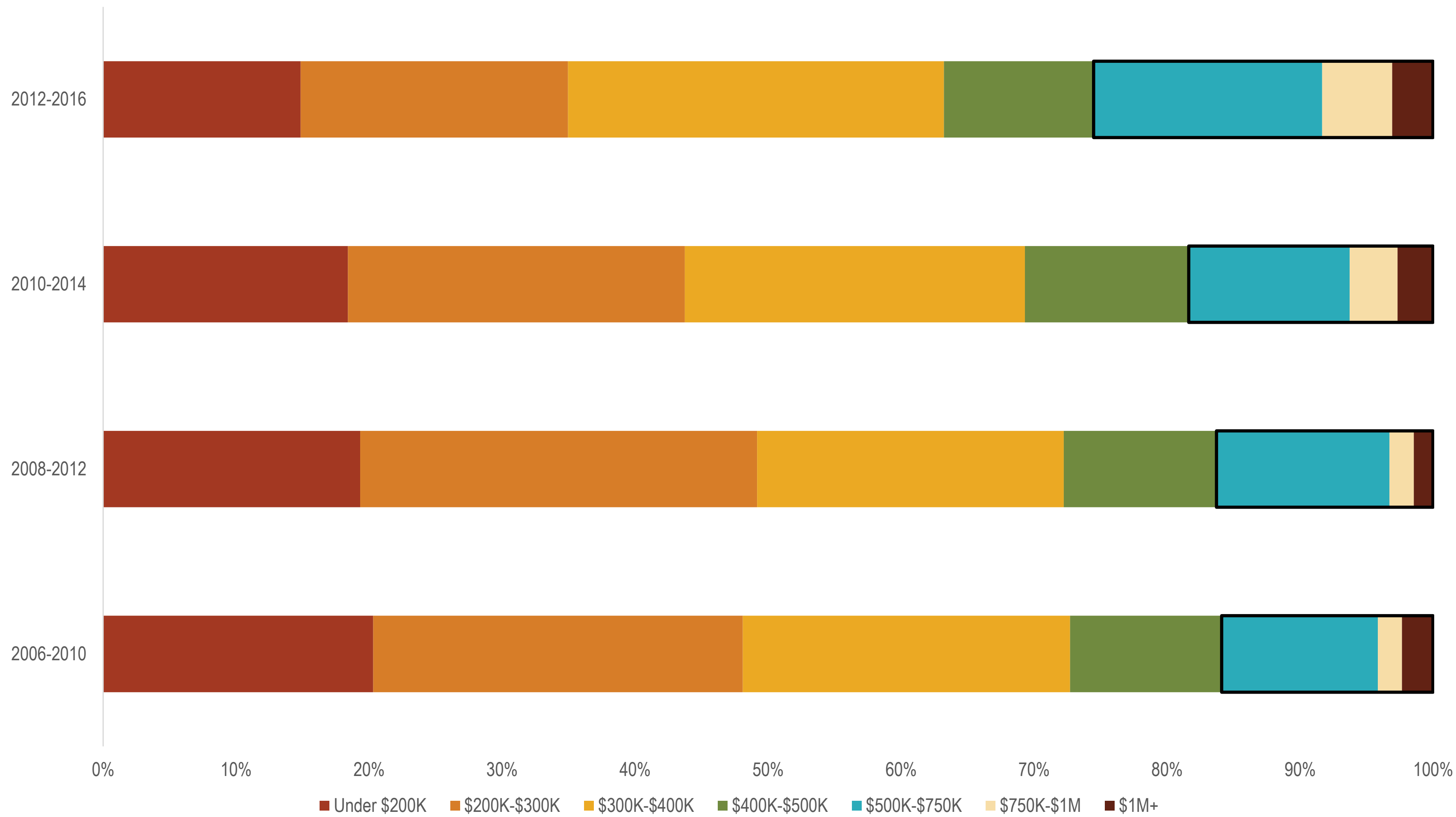
Change in Median Owner-Occupied Home Value
Southwest / Waterfront Census Tracts and Washington, D.C.
2006-2010 to 2012-2016



SOURCE: American Community Survey 2010 and 2016 5-Year Estimates

Exhibit 5

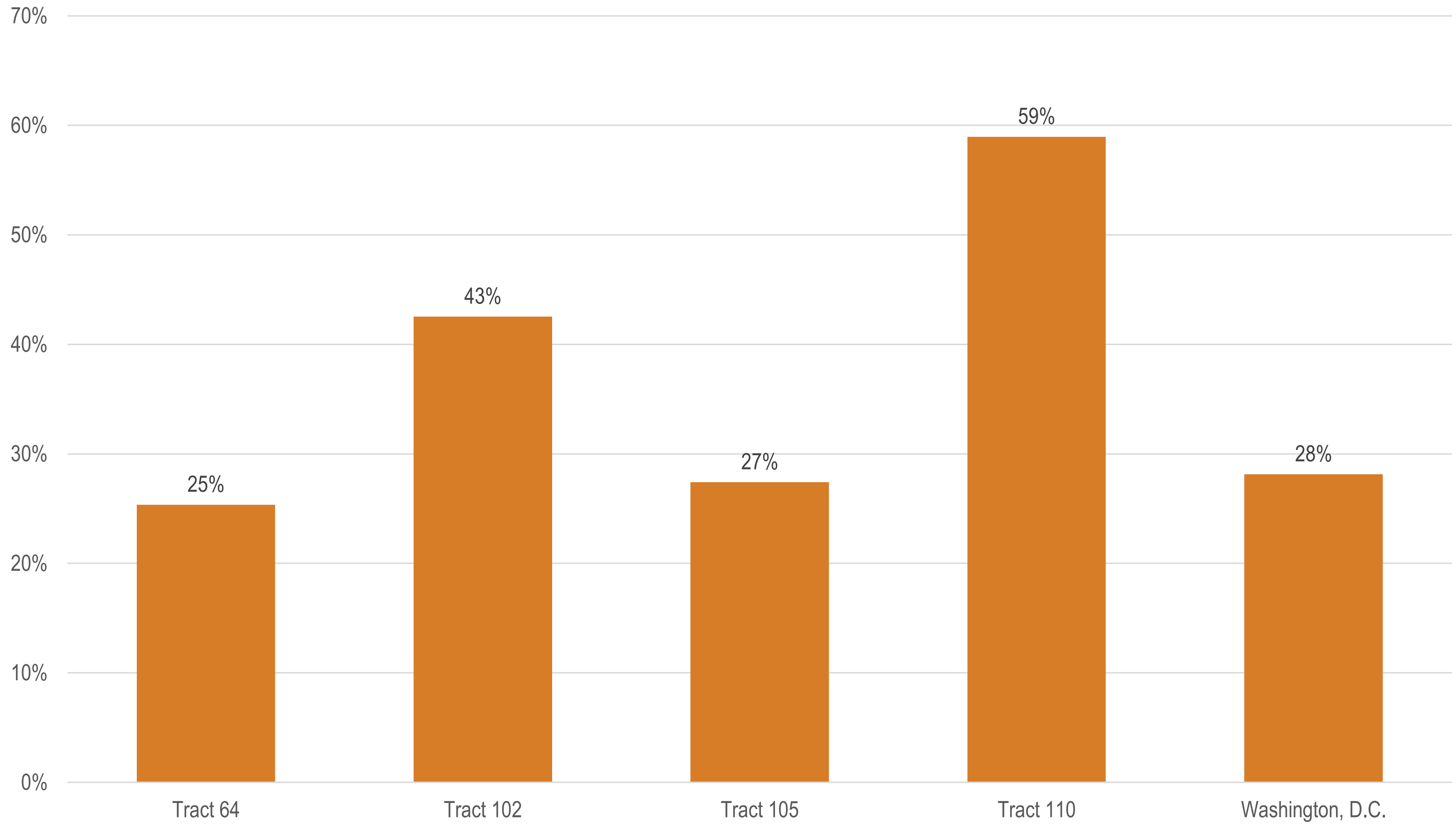
Owner-Occupied Home Value by Price Band
Southwest / Waterfront Census Tracts
2010, 2012, 2014, and 2016 American Community Survey 5-Year Estimates



SOURCE: American Community Survey 2010, 2012, 2014, and 2016 5-Year Estimates

Exhibit 6

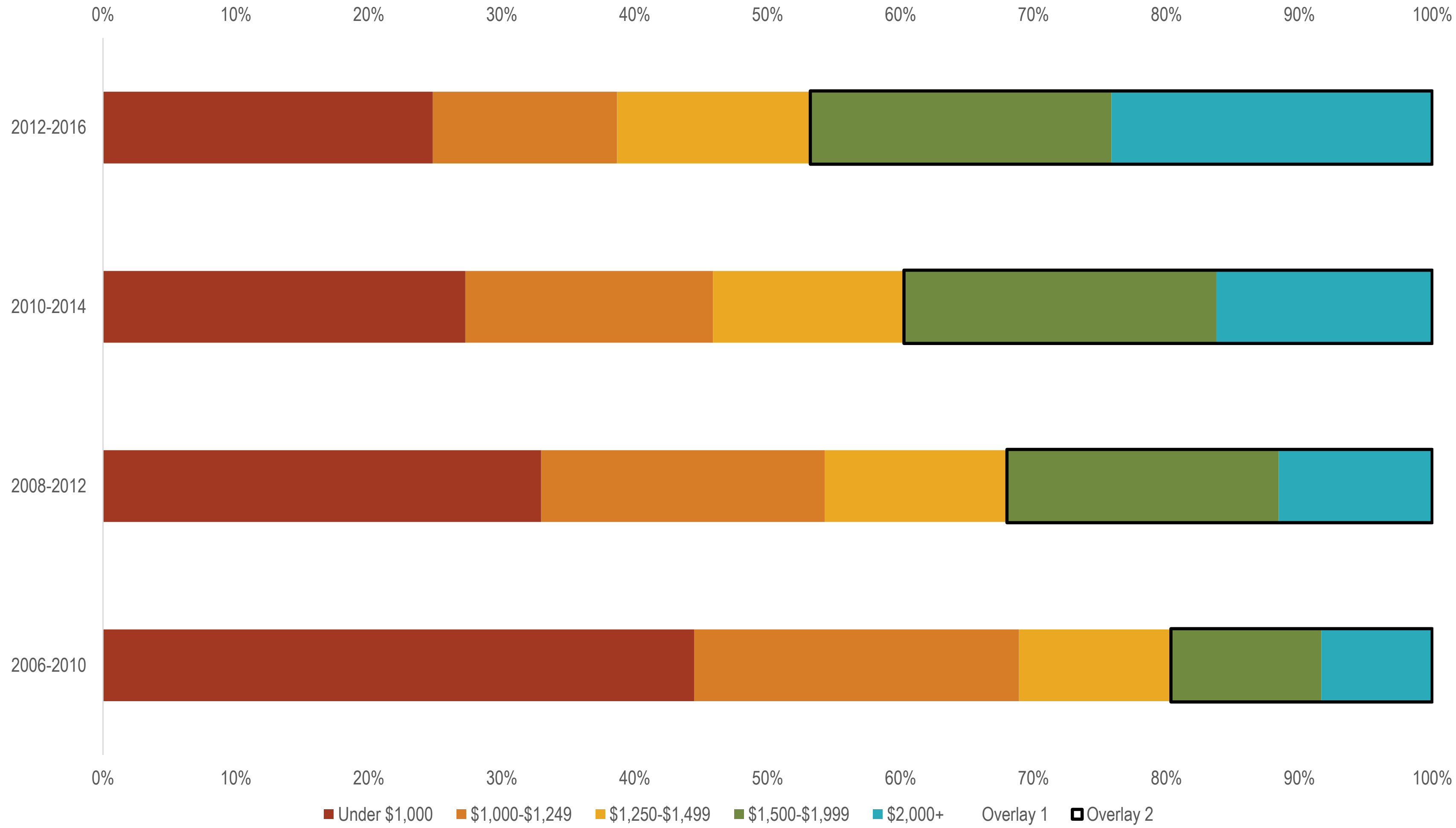
Increase in Median Monthly Gross Rent
Southwest / Waterfront Census Tracts and Washington, D.C.
2006-2010 to 2012-2016



SOURCE: American Community Survey 2010 and 2016 5-Year Estimates

Exhibit 7

Monthly Gross Rent by Price Band
Southwest / Waterfront Census Tracts
2010, 2012, 2014, and 2016 5-Year American Community Survey Estimates



SOURCE: American Community Survey 2010, 2012, 2014, and 2016 5-Year Estimates

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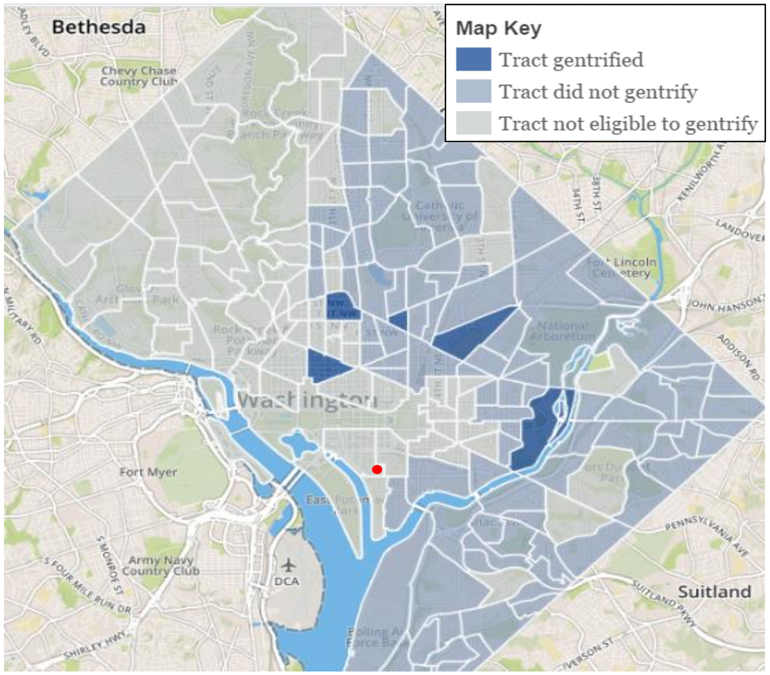
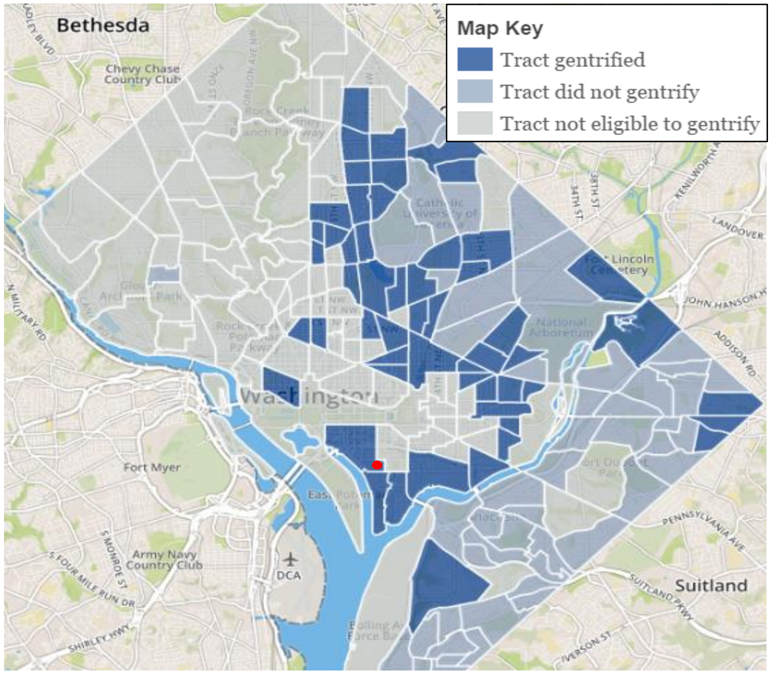
Exhibit 8

Census Tracts That Gentrified
Governing Gentrification Study; Washington, D.C.
1990-2000 and 2000-2013

GENTRIFICATION MAP: 1990-2000



GENTRIFICATION MAP: 2000-2013



=Waterfront Station II Site

SOURCE: Governing; Data sourced from 2009-2013 American Community Survey and 1990 and 2000 U.S. Census