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The economics of homelessness in Seattle and King County

Can a rising tide lift all boats? Here is a quick primer on the state of play in one fast-growth market.

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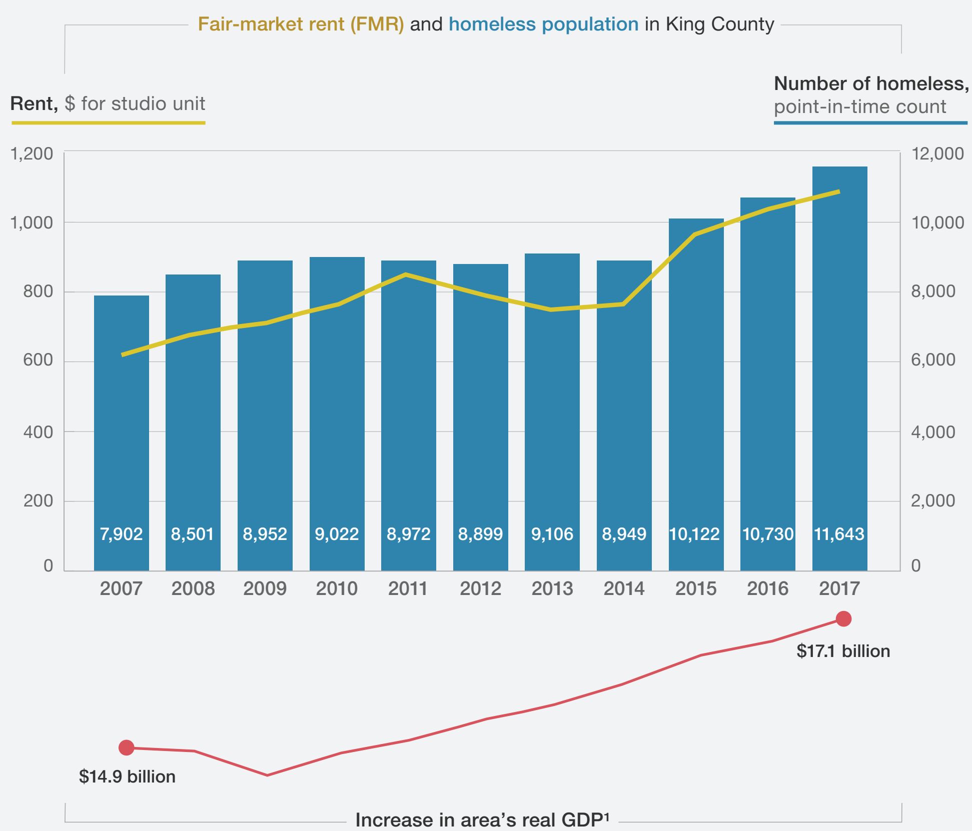
Affluent coastal cities, such as Seattle in King County, Washington, are experiencing a downside of economic growth—rising homelessness. On a single winter night in 2017, volunteers counted 11,643 people experiencing homelessness in King County, a number that represented an increase of more than 9 percent a year on average since 2014. Almost half were sleeping outside rather than in an emergency shelter.

The rise in homelessness cannot be explained by population growth or rising poverty, as there has been little of the former, and the latter has fallen. Exhibit 1 suggests the real cause. It shows how homelessness has risen in line with the fair-market rent (FMR), which in turn has increased in line with the county's strong economic growth. During the financial crisis of 2008, when poverty and

Exhibit 1 Rent increases in Seattle's King County show a strong correlation with homelessness.



[1]Real GDP for January 1 of each year, measured in 2009 dollars, not seasonally adjusted.
Source: Fair-market rents and point-in-time (PIT) count from US Department of Housing and Urban Development; King County 2017 PIT count administered by All Home; US Federal Reserve Economic Data

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unemployment rose, homelessness was relatively stable. But when the economy took off in 2014, so did rents. Since then, the FMR has risen by more than 12 percent a year on average.

The result is a dearth of affordable housing and hence rising homelessness. And without a new approach to the crisis, it can only deepen.

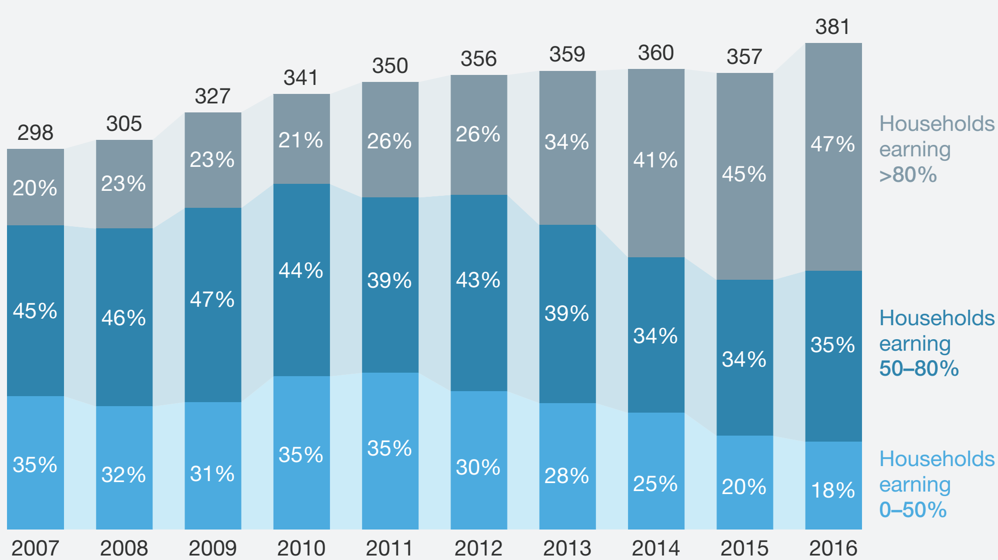
Disappearing affordable housing

There are many triggers of homelessness—an unexpected expense, the loss of a job, poor health, and domestic violence among them. But the rapid decline in the stock of affordable housing means that when people lose their homes, many of them find it hard to find a suitable alternative. As one emergency-shelter provider said, "Ten years ago, our community had pockets of cheap motels and apartments. When you hit rock bottom, you could still find a roof. Today, there is no safe place for people to fall to. When crisis hits, you fall to the street."

The dwindling availability of affordable housing reflects the dynamics of the construction industry. When economic growth is strong, housing developers tend to build more profitable, expensive homes. As a result, expensive homes have become a larger percentage of the available supply in King County. Since 2011, the proportion of units deemed affordable to households earning 80 percent or more of the area median income (AMI) have more than doubled.[1] At the same time, those affordable for households earning 50 percent or less of the AMI have almost halved (Exhibit 2).

Exhibit 2 Supply of affordable rental units by area-median-income tier in King County

Number of rental units,[1] by area-median-income tier,[2] thousand



[1]Figures may not sum to 100%, because of rounding.
[2]All estimates shown are midpoints of confidence intervals.

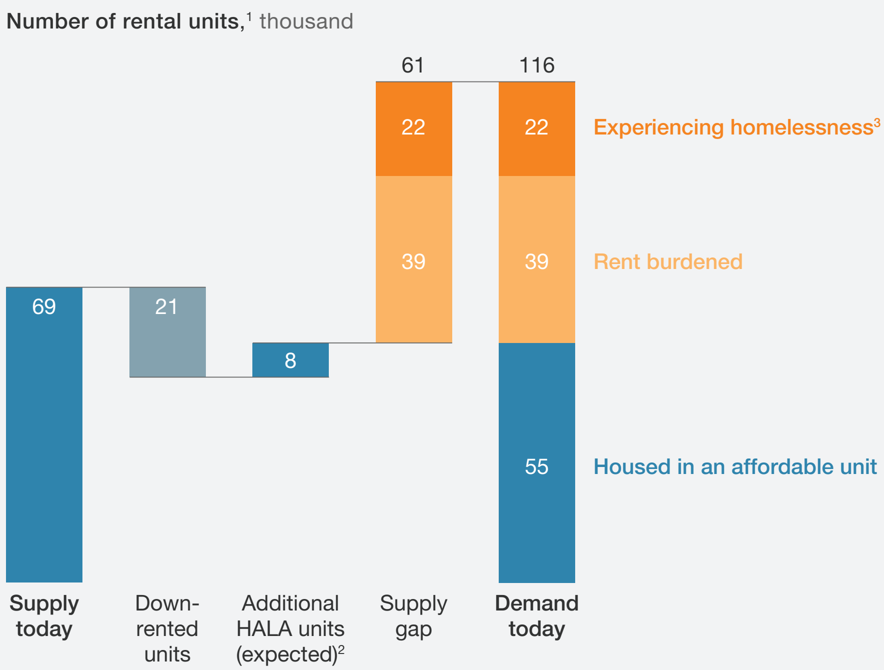
McKinsey&Company | **Source:** American Community Survey Public Use Microdata Sample

Meanwhile, the homelessness-crisis response system, the providers and shelters led by All Home King County, has dramatically improved its performance and efficiency in recent years. With a 35 percent increase in exits from homelessness over 2016, the system permanently housed 8,100 households in 2017. However, given the shortage of affordable housing options, the performance increase of the crisis response system is unlikely to sustain—there are fewer and fewer units available to house people.

As things stand, homelessness in the county could very well worsen. The shortage of suitable permanent housing for people experiencing homelessness is already acute. Although the county's annual "point-in-time" count identified more than 11,000 people needing housing on a single night, as many as 22,000 households sought help from the county's homelessness services across the full year of 2017 at a time when only 8,000 permanent homes were available. Yet even these figures mask the true extent of the shortage.

Exhibit 3 illustrates the point. In 2016, 116,000 households in King County had income of less than 50 percent of the AMI, but there were enough

Exhibit 3 Supply of affordable rental units for households earning 50 percent or less of the area median income in King County



[1]Figures may not sum to totals listed, because of rounding.
[2]Reported additional Housing Affordability and Livability Agenda (HALA) units data only include fraction of units that would be affordable to a 0–50% area-median-income (AMI) household (eg, those built with Low-Income Housing Tax Credits). Additional affordable units might become available through housing initiatives outside of HALA in greater King County.
[3]Assumes all households experiencing homelessness are part of the 0–50% AMI tier. 2017 Homeless Management Information System entries and exits are full-year estimates based on data from 3 quarters.
Source: HALA gap analysis (6000-9000-5000); HALA report; King County Comprehensive Plan, Housing Appendix

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affordable homes for only half of them given that they had to compete for housing with people on higher incomes who “down rent.” Even assuming, somewhat unrealistically, that all new affordable housing currently planned by the city of Seattle was made available without delay, we estimate there would be a supply gap of 60,000 homes. That leaves not only 22,000 households already without a home but another 39,000 living in accommodations they struggle to afford and hence at risk of becoming homeless should their financial circumstances take a turn for the worse.

How to solve the crisis?

A more efficient homelessness response system could be part of the solution. Progress has already been made: the number of people housed annually in King County has doubled since 2013. Resource optimization is a challenge, though. All Home King County, an independent body, is charged with setting out a strategic plan for the various city, county, and philanthropic homelessness funders in King County and measuring results. But it has no authority over these stakeholders, an issue that makes it difficult to avoid redundant efforts that might lead to waste.

But even the most efficient response system will fail without more money. Spending on homelessness has increased but not enough to keep pace with the scale of the problem. Between 2014 and 2017, the number of households accessing homelessness services grew by an average 11 percent a year. Funding grew by an average 2.4 percent a year.

To gauge the extra resources required, we looked at how much it would cost to house the 22,000 households in need with immediate effect. Shelters and other support agencies would likely need more funding, but the bulk could go toward expanding the supply of housing through existing programs, such as Rapid Rehousing, Permanent Supportive Housing (PSH), and the Housing Resource Center (HRC). The first two programs subsidize rents to make unaffordable units affordable and has proved particularly effective in King County. The HRC connects households with private-market landlords, providing light-touch support to the former and insurance against rent defaults to the latter. The YWCA housed as many as 500 households a year through this program before it was shuttered in 2017.

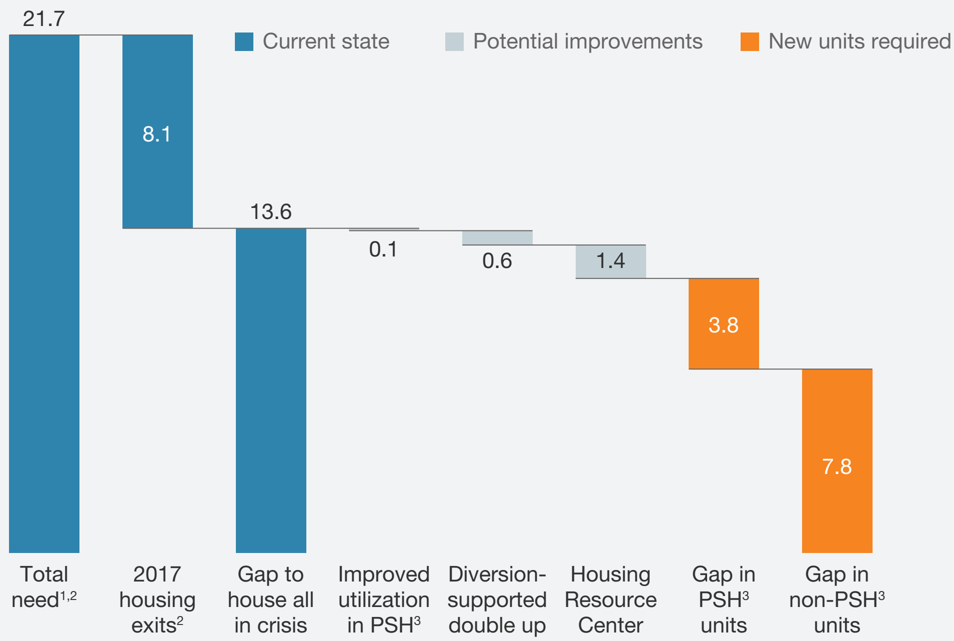
In total, we estimate a budget of $360 million to $410 million would be needed (Exhibit 4). This is about twice what the system invests today. (In 2017, $196 million was spent on the Crisis Response System, leading to 8,100 exits from homelessness and the sustained support of some 4,000 PSH residents.) But it is still less than the $1.1 billion that homelessness is estimated to cost the Seattle-area economy as a result of extra policing, lost tourism and business, and the frequent hospitalization of those living on the streets.

It remains, however, that a budget this size addresses the symptoms of homelessness, not its causes. In the longer term, more affordable homes might need to be built. It is easy to list potential supporting tactics, such as new approaches to building, changes to zoning regulations to allow higher-density housing, incentives for builders, and more publicly owned housing. Each obviously comes with a number of economic and political trade-offs that were outside the scope of our analysis.

King County is not alone in facing a homelessness crisis. As economies grow and affordable housing diminishes, other affluent West Coast cities are experiencing the same phenomenon. A night count in Los Angeles last year identified 55,000 people sleeping outside or in shelters. Builders, businesses, philanthropists, government, and housing providers in King County and beyond should therefore work

Exhibit 4 A combination of strategies might be needed to exit homelessness and move into permanent housing.

Housing options and interventions for those exiting crisis, number of households, thousand



Cost, $ million	196[4]		<1	1	6	73–109	80–96	**360–410 total**

Note: Housing-option costs are inclusive of improvements to Crisis Response System (eg, increased funding for diversion) required for exiting 13.6 thousand households from crisis. Figures may not sum to totals listed, because of rounding.

[1]Homeless Management Information System (HMIS) data of 21.7 thousand households experiencing homelessness are best available data, as suggested by King County. We used 15% range of 18.5 thousand–21.7 thousand given potential for duplication in HMIS and Coordinated Entry for All systems and those households not meeting King County definition of homelessness (eg, doubled-up households).

[2]2017 HMIS entries and exits are full-year estimates based on 3 quarters of data.

[3]Permanent Supportive Housing.

[4]$196 million in 2017 funding includes sustained housing and services for >4,000 existing Permanent Supportive Housing residents.

Source: 2017 point-in-time count; All Home King County inflow estimates; All Home King County quarterly dashboard; King County PSH scattered-site data (Jan 2018); McKinsey analysis

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together if they are to find a sustainable solution to the homelessness crisis plaging their cities. ■

[1] The US Department of Housing and Urban Development defines affordable units as requiring no more than 30 percent of household income.

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