

**BANKING & FINANCE**

Living Small: The Tiny House Trend

Not everyone aspires to live in a big house—some aspire to do quite the opposite. Economy Matters' "ViewPoint" looks at the growing tiny house movement.

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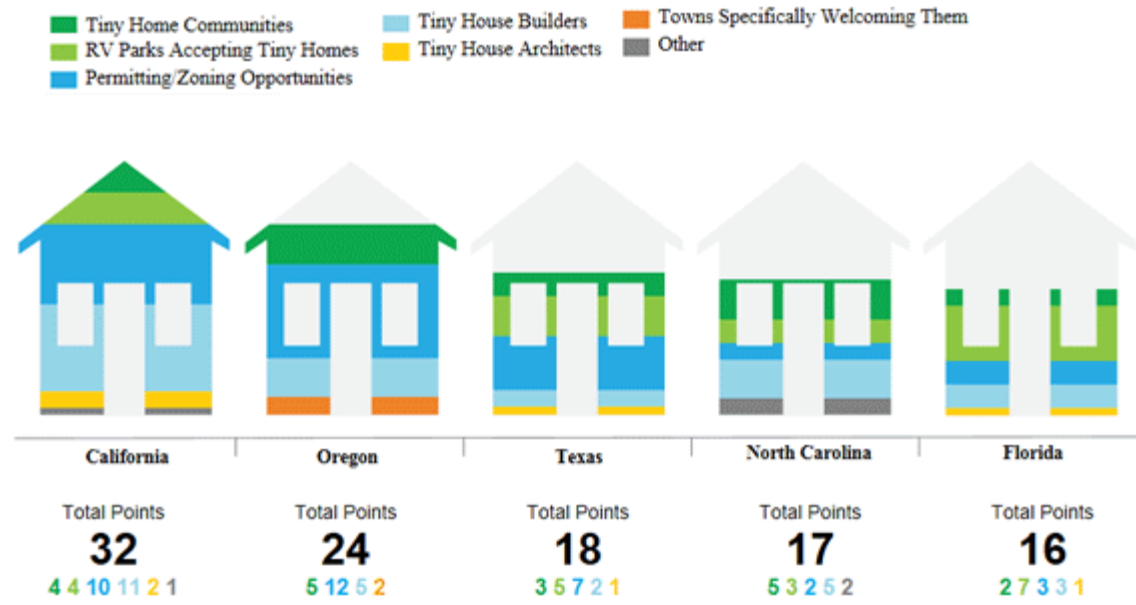
With a new generation entering the workforce with higher debts and lower wage expectations and another generation retiring on limited incomes with little savings, many people are seeking alternative living arrangements beyond the basements of family members. Tiny houses are becoming a new national infatuation as housing costs continue to rise and people scramble to find more affordable housing. Popular shows on cable television also extol the virtues of living in a limited space.

Although there is no standard definition of a "tiny house," floor plans with 400 square feet or less are generally included in the tiny house category. Tiny houses usually consist of one room, with a sliding-door bathroom in a corner, and perhaps a loft bedroom. Many tiny homes are not built on permanent foundations; instead, they are built on trailers with wheels.

Small houses, growing movement

Tiny house communities are popping up in certain sections of the country. The small city of Spur, Texas, is believed to be the first U.S. city that allows homes smaller than 500 square feet to be located anywhere within its boundaries. Portland, Oregon, and Seattle, Washington, are viewed as tiny house-friendly urban areas. According to ecobuildingpulse.com, which assigned a point value for various key indications that a state would welcome a tiny house community, California ranks as the best location and Florida ranks fifth overall (see the graphic).

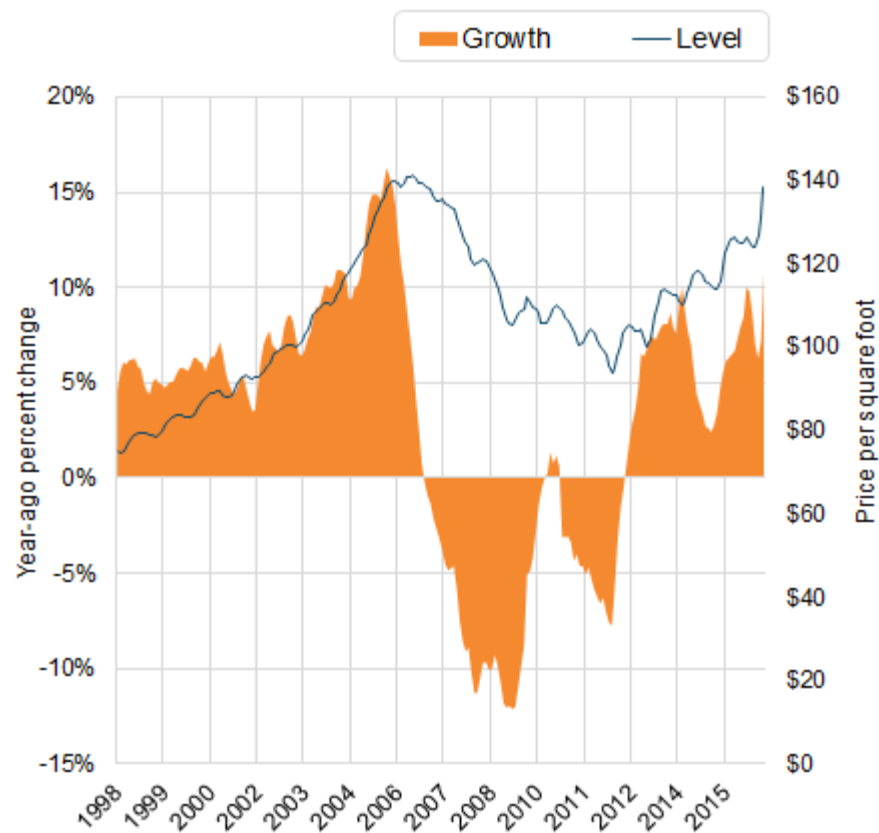
Top 5 States for Tiny Homes



Source: ecobuildingpulse.com

Although the tiny house market accounts for less than 1 percent of real estate transactions and appears unlikely to become a mainstream way of living (according to the U.S. Census Bureau, in 2010, the median square footage per house in the United States was 2,100 square feet), both young adults and retirees are exploring the option. As mentioned, one of the biggest appeals of tiny houses is their affordability. According to Zillow, in December 2015, the median U.S. home value was \$183,500. As the chart shows, the median sales-to-square foot value has trended upward since the financial crisis and recession. In comparison, the average price of a tiny home is roughly \$23,000. For people willing to build it themselves, tiny homes can cost as little as \$10,000 to construct.

U.S. Median Home Sale Price per Square Foot



Source: Zillow and the Atlanta Fed's Risk Analysis Unit

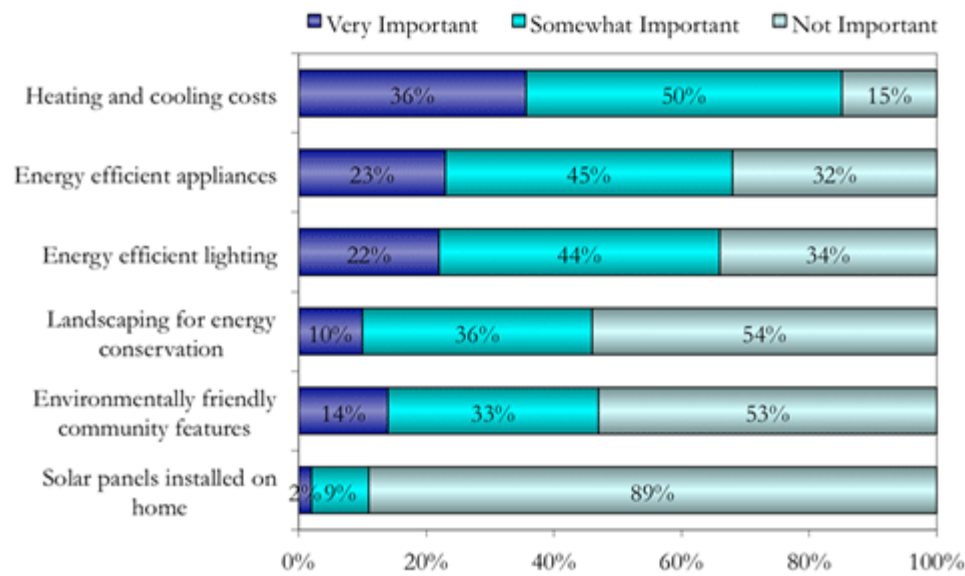
Environmental aspects spurring interest

A second reason that tiny houses are appealing to buyers is their environmentally friendly features (see the chart below). A poll conducted by the Washington Post found that 76 percent of millennials consider climate change a serious problem facing the country. It's not surprising, then, that buyers are indicating, through surveys such as the Profile of Home Buyers from the National Association of Realtors, that reducing the environmental impact of their home is an important consideration in purchasing a house. Many buyers are looking for energy-efficient appliances and lighting and landscaping that is consistent with soil conservation. Tiny houses require fewer raw materials and less energy to heat and cool. Greenhouse gas emissions from tiny homes are 14 times lower than from average houses. Given these features, tiny houses fit in with the lifestyle that some millennials are seeking.

Challenges to tiny home ownership

Although tiny houses have piqued the interest of buyers, there are several potential hurdles to tiny house ownership, including obtaining financing and complying with city ordinances and neighborhood covenants. Large mortgage lenders typically do not offer mortgages on tiny homes because of costs and collateral values of the tiny houses. In terms of costs, whether a mortgage is for \$23,000 or \$230,000, loan origination and servicing costs are about the same, so banks may be unable to make profitable mortgages on tiny homes. Banks' underwriting standards

Environmental Concerns



Source: 2014 NAR Profile of Home Buyers and Sellers

ownership. Zoning laws typically require homes to be at least 500 square feet, effectively making tiny homes illegal in many cities and suburbs. One loophole to the size requirement may be found in cities that allow small secondary residential spaces, known as accessory dwelling units (ADUs), on lots. The challenge with using this loophole is in finding an owner willing to allow a tiny house to be placed on their property. In addition, cities that allow for ADUs often require the unit to be built on a foundation, while many tiny houses are on wheels.

A second hurdle faced is gaining acceptance from existing homeowners, many of whom may have restrictive covenants to protect their property values. Covenants may require that a home be of a certain minimum size or that the foundations be constructed in a particular way to avoid diminishing property values, which effectively prohibits tiny house construction. Many neighborhoods also ban mobile homes and renewable energy technologies, such as solar panels and wind turbines, which appeal to tiny house buyers.

A growing market for shrinking homes?

Although tiny houses may be capturing the imagination of people looking for an affordable living space, the market for such homes is likely to remain small. Financing options are limited, as are the areas in which tiny houses can be located. Families with children will most likely continue to opt for houses with larger floor plans. Some builders are beginning to construct traditional homes in more environmentally friendly ways, which may also attract potential tiny house buyers concerned about their environmental impact.

may also limit the number of low-cost originations. It is still possible to obtain a mortgage. However, typically it will be through smaller institutions, such as community banks, where the customer has a long-term relationship, or credit unions. There are other bank options for financing the purchase of a tiny house, including obtaining an unsecured loan or a secured personal loan, such as an RV loan. However, in order to obtain an RV loan, lenders may require that the tiny house be certified by the Recreational Vehicle Industry Association.

Even if obtaining financing is not an obstacle, local zoning laws and neighborhood covenants regarding land use can be a barrier to

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