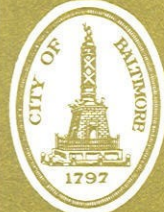


*Andrew Klein*

FROM	NAME & TITLE	Andrew Klein, Chief	CITY of BALTIMORE <b>MEMO</b>	
	AGENCY NAME & ADDRESS	Bureau of Budget and Management Research Department of Finance		
	SUBJECT	City Council Resolution No. 09-0136R – Investigative Hearing- Urban Modular Home Factory		

TO

DATE: June 30, 2009

Honorable President and  
Members of the City Council  
C/O Karen Randle  
Room 409, City Hall

This resolution explores the feasibility of Baltimore City creating and operating an urban modular home factory.

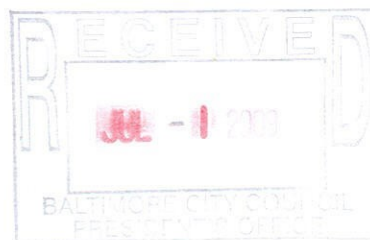
The Finance Department makes no judgment on the method or quality of construction, as that is a market function and those questions are best answered by the Department of Housing and Community Development. The general fiscal impact on the City is discussed first in terms of economic impact, next in terms of tax and expenditure impact and finally in terms of capital and operational costs of the factory.

### **Economic Impact**

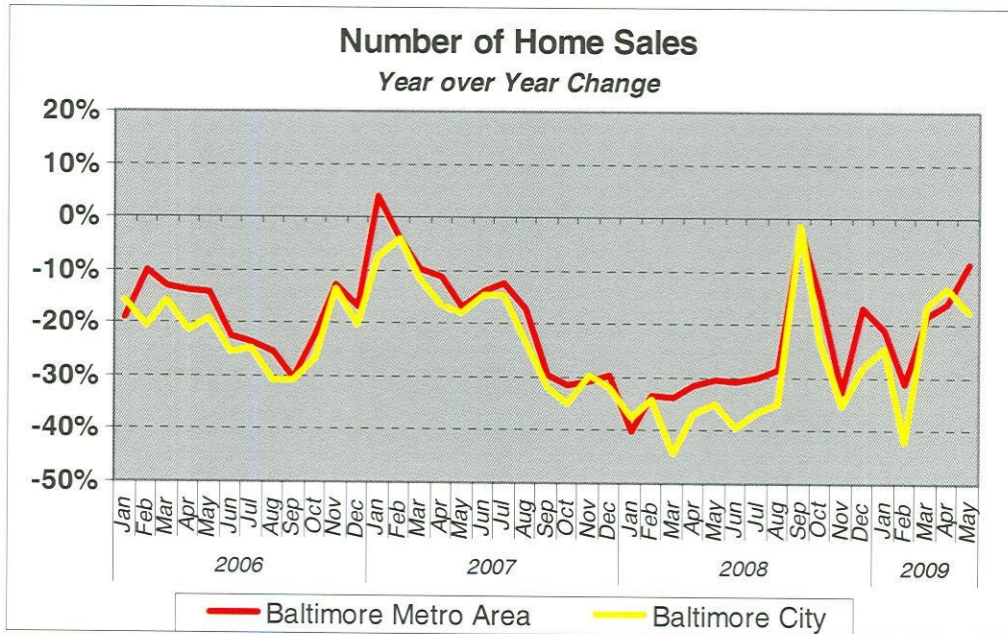
Housing inventory is currently at an all time high and at the same time demand for housing is decreasing. Although the decrease in demand in Baltimore has slowed in the last couple months, the chart below shows that the current level of home sales is still almost 20% below last years levels. Nationally, new home sales in May 2009 declined 0.6% from the prior month and decreased 32.8% from the prior year, to 342,000 (BEA).

Additional new housing stock will have the effect of driving down current prices and potentially retarding or stagnating recovery of Baltimore's current housing market. Lower housing prices will result in lower property tax assessments and lower property tax returns.

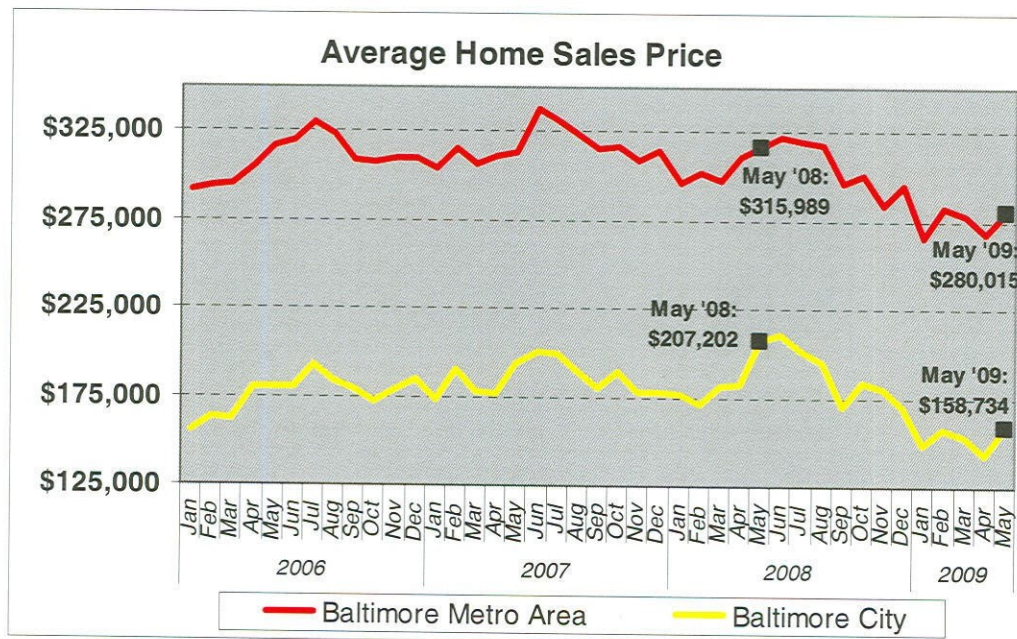
On the other hand, redevelopment of existing vacant housing stock will tend to have a positive effect on neighborhood prices and offset price declines due to increases in supply.



*Comest*



*Employment-* The establishment of an urban modular home factory would result in a need for factory workers, but it is believed that these workers would merely replace construction workers that are currently producing site constructed housing, so no net gain in employment would be realized.



### **Fiscal Impact**

*Property Taxes* – The resolution estimates that the factory could produce 30,000 new homes over the next ten years. If these homes are in addition to homes that would normally be constructed, a net gain in property tax would be realized. It is the opinion of the Finance Department that the modular homes would be replacements to homes that would have been built if no modular factory were developed. If construction of modular homes merely replaces the demand for site built homes, no new property tax revenues would be realized.

The Finance Department also questions the demand for 30,000 additional homes in the City given current inventory levels. If demand existed for 30,000 new homes, we would assume that the private sector would be interested in meeting that demand. As an indicator of demand for new housing, we can look at applications for the Newly Constructed Tax Credit (this also includes redeveloped housing). On average 225 persons a year have applied for and received this tax credit. We believe that this tax credit provides us an indicator of the demand for new housing.

Even more problematic is the cost of the modular homes per square foot. Currently the average cost per square foot in Baltimore is \$128 (Trulia.com). Based on the numbers referenced in the CCB 09-0136R for the City of Detroit, we have estimated the costs to be approximate \$148 per square foot. Such homes would be at a competitive disadvantage when compared to the cost per square foot of existing stock.

At \$148 per square foot, an 800 square foot home would require an estimated income of \$37,000 per household in order to obtain a mortgage under FHA guidelines. Based on the U.S. Census 2007 median household income of \$36,894 for Baltimore, over half of the households in the City would not qualify for a mortgage under these guidelines.

*Other taxes and expenditures*- While receipts from other taxes would increase, they are not expected to be significant when offset against additional expenditures required to support the new homes. Estimating expenditures is difficult not knowing the location and density of development. If the homes were clustered together in “new” developments, additional services would be required at the outset. On the other hand, if the new homes are spread throughout the City, existing services would be able to service the residents with marginal expenditure increases over time.

### **Feasibility of Creating and Operating an Urban Modular Home Factory**

It is difficult to estimate the cost of a modular home factory. Substantial capital costs would be incurred to purchase land, buildings and equipment. Product engineering costs would also be required along with an initial inventory of raw materials. A team

of modular experts would need to be hired to oversee start-up of the factory. Additionally, a market analysis would need to be performed to determine where the vacant lots are located and if they could support the price that would need to be charged in order for the city to break even on the full cost of a modular home.

Operational costs, including employee salary and benefits, taxes, utilities, materials, transportation, insurance (liability and property) and marketing would need to be financed until sales receipts could cover these expenditures.

Because many of the vacant lots are in areas that limit the price of a home, the City may need to look at subsidizing construction or land costs. This could result in a net loss for some homes built.

Furthermore, assuming the City were to build 3,000 homes a year for the next 10 years filling all vacant lots, the City would then be faced with the sale or closure of the modular home factory. It is questionable that all capital cost could be recovered in such a short period of time. Historically, over the last decade, governments have divested themselves of enterprises such as these and outsourced these functions to the private sector.

#### Recommendation

It is the Finance Department's position that the private sector is best equipped to efficiently provide Baltimore City with new housing construction and unless a clear market failure exists, the City should not compete with the private sector construction industry.

As alternatives, the Finance Department would suggest that the Department of Housing and Community Development explore a partnership with a modular home manufacturer for specific modular home projects such as the City of Detroit's "Next Detroit Neighborhood Initiatives." The City might also explore the relocation of an existing modular home factory to Baltimore City.

CC: Edward J. Gallagher  
Angela Gibson

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