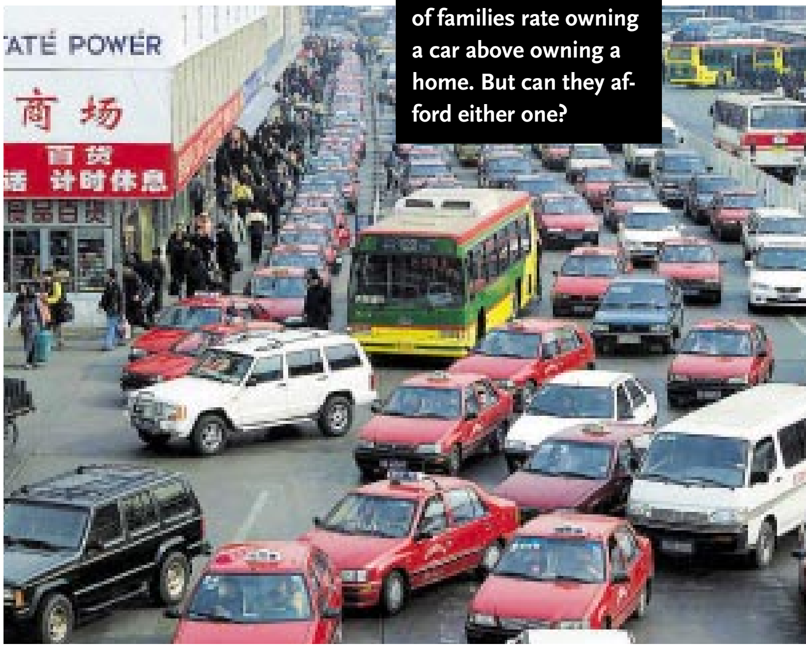
observations

Jetta-ing into debt



SHOW ME THE MONEY

In Beijing, 64 percent of families rate owning a car above owning a home. But can they afford either one?

In Beijing, nothing screams, "Look at me!" like a flaming red Volkswagen Jetta. China's astounding growth over the last decade has been reflected in urban incomes. With elevated incomes comes the quest for elevated status, and there is no better symbol of status than a shiny new automobile.

But how all of the 1 million people who bought new cars in China last year managed to afford their purchases is puzzling. In the 1990s, passenger cars were the toys of privileged elites, who would simply walk into the dealership hauling a briefcase full of cash. Today's Chinese car buyers are increasingly likely to be members of the growing middle class, and they come to dealers with something else—loan papers. In 2002, a record 20 percent of Chinese car buyers financed their aspirations with a bank loan, fueling a 55 percent annual increase in auto sales.

The problem is, the prices of new cars far exceed the incomes of those purchasing them. The top two sellers in China last year—the Jetta and the Santana—retailed for between $25,000 and $40,000 after adjusting for price differences. Yet in Beijing, 60 percent of families with an annual income of $5,000 or more plan to buy a car, and the average Chinese household feels that it can afford a new car at an income of about $9,600. Borrowing the typical 50 percent for a 60-month loan on a new Jetta, a household earning $9,600 per year would be forced to commit 35 percent of its income to car payments *before interest*. And that's after the down payment and registration, which together can exceed $20,000.

STATUS SYMBOL

Cost of most popular new car as a percentage of average annual income, 2002

Japan	21%
United States*	34
Italy	48
Mexico*	182
China	1,622

* 2001
SOURCES: Manufacturers' data, national statistical agencies, and BBC

What happens to car buyers who take on more debt than they can handle? The short answer is…who knows? Many owe large debts not only to banks but also to friends and relatives who helped to finance the down payment. Many more exhaust huge portions of their savings to meet the steep up-front costs. Banks reserve the right to repossess the cars of borrowers who do not make payments, but with an underdeveloped legal system, there have been very few lawsuits. Is the Chinese car market an accident waiting to happen? —*Kristina Johnson*

Take home pay

The purchase of a home is a financially momentous step for a first-time buyer. In the greater Boston area, where the median selling price of a single-family home exceeds $415,000, this step may be too large for many young families to take. Recent economic developments such as low interest rates and new mortgage programs for first-time homebuyers have brought some families within reach. But the homeownership rate in Massachusetts, at 60.6 percent, still lags more than 7 percentage points behind the nation's.

Over the last decade, a solution has emerged that solicits help from an alternative source—employers. About one in seven employers nationwide offers some sort of housing assistance to their workers, according to a recent study by the Society of Human Resource Professionals. For instance,

illustration by adam mccauley, photograph by corbis images

Bentley College in Waltham, Massachusetts, offers their employees access to mortgage service and real estate benefits programs. Other area employers, like Citizens Bank and MassEnvelope Plus, are providing forgivable loans and generous mortgage rates to their employees. Employers see benefits for themselves and for their employees stemming from these programs, such as higher retention rates, greater job satisfaction, and a competitive edge in the quest to attract high-quality applicants.

As a long-term solution to the affordable housing problem, though, the benefits of employer-assisted housing are less certain. The programs currently help only a small proportion of the workforce; for instance, just seven companies have signed up for a Greater Boston Chamber of Commerce program introduced last year to help businesses set up employer-assisted housing. In addition, they take time to organize and can involve substantial legal and administrative costs. And it's particularly hard to convince employers to take on this additional cost during an economic downturn, when competition to attract workers is less fierce.

But perhaps most importantly, these programs do not affect the supply of housing. Two years ago, vacancy rates for owner-occupied housing in the Boston area dropped to a level of 0.6 percent, well below the 2 percent that is considered normal. Increases in supply since then have been minimal, exacerbating an already tight housing market. While employer-assisted housing programs may allow companies to help their own workers with housing issues, it remains to be seen whether the programs can contribute substantially to resolving Boston's affordable housing problem.

—Jennifer Young

WRITE TO US *We are interested in hearing from you. Please address your letters to: Federal Reserve Bank of Boston,* Regional Review, *P.O. Box 2076, Boston, MA, 02106-2076. Or send us an email at jane.katz@bos.frb.org.*