The Future of Accessory Dwelling Unit (ADU) Financing

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ADU Definition
- Additional living structures on single family or multi-family lots
- Can be new structures, garage conversions, or a separate part of the primary dwelling
- Includes a kitchen and bathroom

Primary Use Cases
- Adult children
- In-laws moving in/residential elder care too expensive
- Rental income
- Increased home value
- Aging-in-place

Legislative Landscape
- In the past several years, many states and municipalities have made ADUs easier to build or harder to object to

Benefits of ADU Asset Class
- Serves as suburban infill
- More NIMBY-proof than other housing forms
- Substitute for building in flood plains and fire prone areas
- Can utilize existing structures
- Can add to housing stock near transit centers in residential areas

Current Financing Options
- Home Equity Loan
- Home Equity Line of Credit
- Cash-out Refinance
- Construction Loans
- Second Mortgage
- Cash/savings
- Loans from family/friends

Shortcomings of Current Financing Options
- Geared toward high-income homeowners
- Geared toward homeowners with higher home equity
- Loan limits are sometimes not high enough to finance an ADU
- Loan limits don’t take into account rise in home value post-ADU construction or ADU rental income

Current Efforts to Expand Financing
- ADU-specific credit union loans
- City-run programs, like LA’s Backyard Home Project and the Boston Home Center ADU Loan program

Future of ADU Financing
- Community Development Financial Institution loans, like Oregon-based Craft3’s ADU loans
- Government-sponsored enterprise ADU mortgage products
- Loans tied to rent ADUs to low-income tenants

ADUs by the Numbers
While cost can vary greatly by metropolitan area, typical ADUS cost between $100-200k, meaning that the cost of financing an ADU is often prohibitive to those who could most benefit from one (see example right).

The graph at right highlights the increase in ADU rental listing in the past two decades, demonstrating that ADUs are not only used by family members, but are also becoming a critical element of the rental housing market.

Recent liberalization of ADU laws in California led to a many-fold increase in ADU permits issued in LA — these numbers (and the units they would add to the housing stock) would likely be higher if more financing options existed.

ADU Permits Issued by Year in Los Angeles, CA

Image from buildinganadu.com