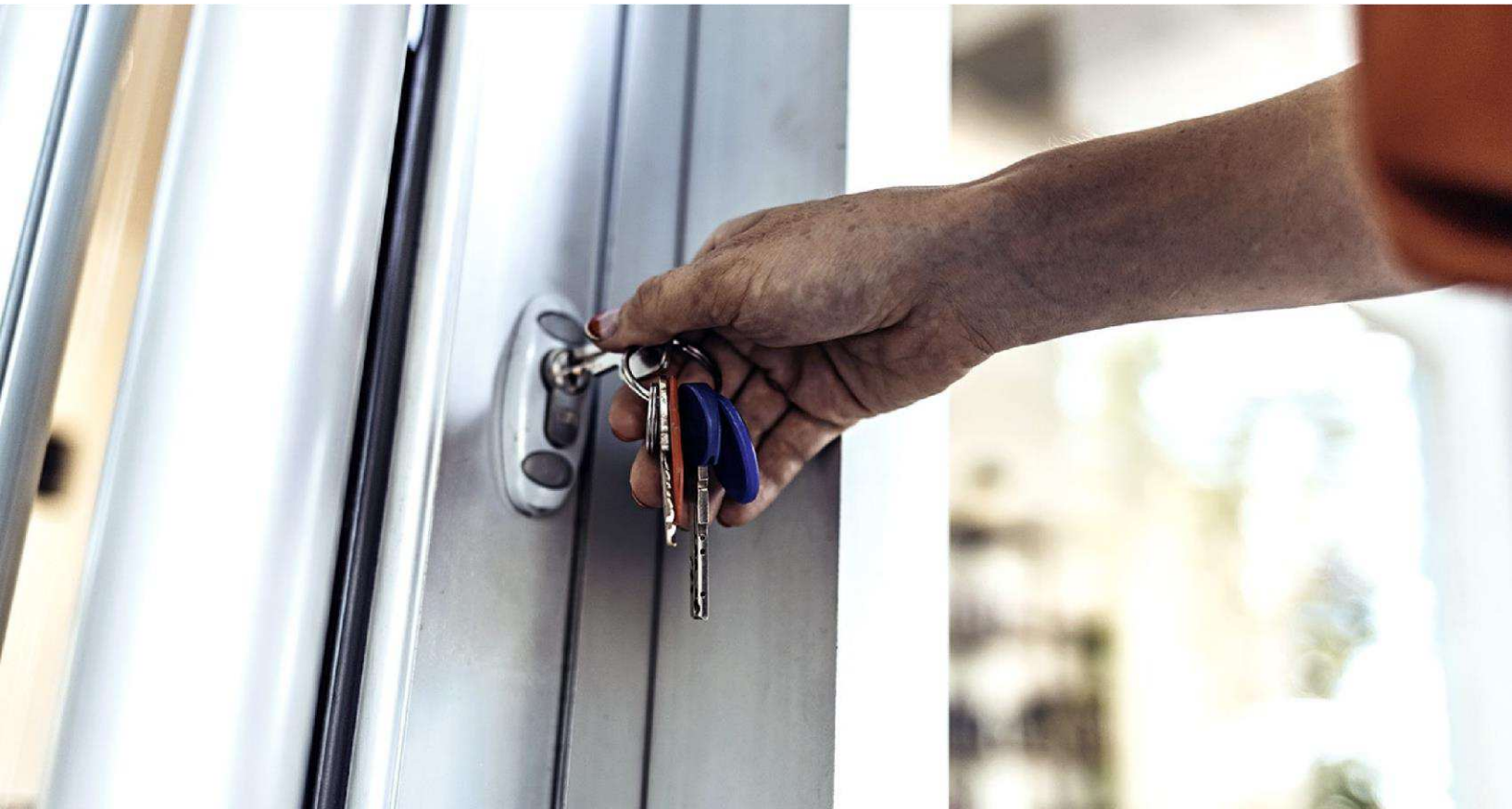


McKinsey Institute for Economic Mobility

Confronting the affordable-housing crisis

US families face a housing shortfall from coast to coast. New research reveals what's at stake if costs continue to escalate, plus what can be done differently to advance meaningful change.



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The US housing crunch is bad—and it's getting worse. Wider access to safe, affordable homes is vital to enabling economic mobility for all Americans and to harnessing what McKinsey Partner [JP Julien](#), a leader of the [McKinsey Institute for Economic Mobility](#), calls a “massive” untapped economic opportunity. On this episode of *The McKinsey Podcast*, Julien joins Global Editorial Director Lucia Rahilly to discuss what's causing the [crisis in affordable housing](#), who's most affected, and what both public and private sector leaders can do to effect fast but lasting change.

The McKinsey Podcast is cohosted by Lucia Rahilly and Roberta Fusaro.

The following transcript has been edited for clarity and length.

What's new on McKinsey.com

Roberta Fusaro: Here's what's new on McKinsey.com. There's a report on [the state of aviation](#), where we learn about the plight of low-cost airlines, aircraft shortages, and how to modernize airline planning. Also out is our annual report about [private markets](#), which continue to face uncertain conditions. Both pieces can be found on our website and in our show notes.

A growing shortfall

[Lucia Rahilly](#): In the US, the cost of having a decent place to call home is becoming out of reach for a rising number of families. JP, you recently coauthored a report on [affordable housing](#) with the [McKinsey Institute for Economic Mobility](#). Talk to us about what's going on.

[JP Julien](#): In the simplest terms, we have a massive housing shortage, and that crunch is really affecting families' ability to achieve more. In 2023, we estimated there were 8.2 million fewer units of housing than the market required to meet the needs of American families. Without action, that number could grow to 9.6 million by 2035.

This gap has huge implications for our economy and for everyday families. It's the reason 40 million American households spend more than 30 percent of their income just to find shelter. That's one in three households spending nearly a third of their income just to have a home as of 2022. If you think about what that means in terms of families' ability to build wealth but also feel secure and develop roots in a place, it has real consequences.

[Lucia Rahilly](#): When we're talking about access to safe, reasonable-quality housing, are we talking about buying or renting or both?

[JP Julien](#): We looked at both, because it's helpful to think about this problem holistically. Whether a family chooses to rent or buy, we believe their ability to do so in an affordable way that meets their needs is critical.

[Lucia Rahilly](#): How and why does location factor into the economic mobility calculus for American families?

[JP Julien](#): Place matters a lot. If you think about what it takes to experience economic mobility, your address plays an enormous role. It's your proximity to a good job, your ability to access healthy food or a bank, childcare or healthcare, your kids' school, or even your exposure to violence.

It involves the extent to which you have thriving green spaces around you, and on the flip side, pollutants that negatively affect your health. Increasingly, it includes your exposure to risk of climate disaster, whether flooding, wildfires, or hurricanes. All those interconnected macro forces are fundamentally shaped by where your housing is located.

The truth is, because we have a lack of housing and a suboptimal way of determining where housing gets built, we create an artificial barrier for millions of families to have the opportunity to achieve upward mobility.

Lucia Rahilly: Raj Chetty, an economist, has done amazing work on this. It seems like even your zip code can make a difference in kids' future trajectory.

JP Julien: Yes, Chetty's work on neighborhood conditions, as well as other scholars' work—the Heckman Equation or the Social Genome Project—all essentially say that the chances that a child experiences economic mobility are fundamentally shaped by the places in which they grow up. Housing must be a fundamental area of impact for us to see changes in economic mobility. **Lucia Rahilly:** And this is a national issue, not just in big coastal cities like New York?

JP Julien: It is everywhere, unfortunately. It's in New York City and in Philadelphia, where I am, but also in rural America. It's on the coasts and it's in inland communities. It is in communities that are majority Black, White, Native American, and Asian. It's facing young adults just entering the workforce and retirees thinking about their next horizon in life.

Lucia Rahilly: Did you find some demographics were more affected than others?

JP Julien: We did. Even relative to some other economic mobility outcomes, Black Americans in particular are hard-hit by the housing crisis. That's driven by two underlying factors.

The first is that Black Americans are overrepresented in the places where housing gaps are the widest. The second is that Black Americans are overrepresented among the lowest-income Americans. And as we see in the data, lower-income Americans face the most downside impact of this housing crisis.

A massive economic opportunity

Lucia Rahilly: Obviously collective well-being has long been a fundamental value in the United States, and you've talked about economic mobility for the populations being affected. Is there a larger economic case for addressing the housing crisis?

JP Julien: The economic opportunity is massive. Addressing the eight-million-to-nine-million-unit housing shortfall that we're facing over the next decade—if solved—could unlock \$2 trillion in GDP and create approximately 1.7 million jobs. That's not even accounting for additional benefits like what those new units would mean in terms of property taxes that could support public investments such as schools and infrastructure.

And while that's a big national number, it also will reverberate locally. If you take a place like Chicago, we estimate that solving this housing crisis unlocks nearly \$30 billion of local GDP and around 27,000 jobs. So, the opportunity for impact for the broader economy is huge.

What's causing the crunch

Lucia Rahilly: What's driving this crisis in affordable housing?

JP Julien: There are three big causes. The first is the cost of land and construction. Land is the single largest driver of housing costs, and we are artificially restricting what can be built on our scarcest resource. About 75 percent of residential land in the US, for example, is zoned for single-family use. If you add that to increasing labor shortages and higher materials costs, you end up with slower production at a higher cost.

Second, there simply isn't enough private capital being invested in affordable housing. There's a bit more complexity with affordable-housing finance, but at face value, affordable housing also has lower returns. Returns are primarily driven by rents: for an investor, the higher the rent, the greater the return. What's often lost is that once you factor in providing affordable housing that people can sustain over time—some of which is subsidized by the federal government—on a risk-adjusted basis, we see quite a bit of upside. But that story hasn't fully made its way through the sector.

Last, there is not enough support for families. The lowest-income families can't comfortably afford housing. More than half are cost burdened today. Ten-plus percent of American households have no wealth or are in debt, including 24 percent of Black households. So, there is not enough money to absorb increasing housing costs or to support housing that is affordable and sustainable.

Lucia Rahilly: How are local zoning laws and communities contributing to the issue?

JP Julien: We [highlight five types of solutions](#) in the report. Zoning is first on the list. We know that it's quite effective, so things like increasing single-family zoning to multifamily or reducing parking minimums or lot sizes—we have good examples showing they work in terms of increasing density, and therefore the affordability of housing.

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The challenge is that what works in one place does not work in another. A big driver of that is local control of zoning. In some ways, it's helpful that you as a homeowner have a sense of what happens in your community: the fabric of the homes that are built, for example. What is left out, oftentimes, is that you end up with either a small number of loud voices or not the right incentives for residents and jurisdictions to adopt more housing-friendly zoning that would increase the number of units and therefore the ability for people to afford them.

Increased density means more different kinds of families living in proximity. What we see in the research is that going to school with people of different incomes is better not just for the lower-income students but also for the higher-income students. It leads to more diverse and interesting cuisines. It tends to lead to more resources to do things like invest in infrastructure—to build sidewalks or fix potholes—and to a higher likelihood of a thriving main street where more businesses serve more residents.

Lucia Rahilly: Is zoning reform largely a question of explaining what these housing-friendly incentives might be? Or are there other incentives that we saw working?

JP Julien: We could definitely use a bit of narrative on the benefits, as opposed to just the drawbacks. There also need to be more incentives. For example, at the jurisdictional level, how do you provide additional funding for local communities that decide to up-zone, particularly upzoning

around transit and other assets? In Massachusetts and Colorado, grant funding is incentivizing zoning in beneficial ways.

The other idea we played around with, which is much more novel and does not yet exist, is ways for existing residents to benefit from zoning. If I'm in a community and I'm opposed to zoning, what if I were able to either directly benefit from or have more of a say in how the incremental resources collected for more housing were spent in my community?

We also know that while zoning can be contentious, a great place to start is to think about what assets and resources state and local governments already own, because to a degree, there is alignment that more housing is probably better. How could these resources be repurposed, particularly around multifamily housing? For example, we did some work for a state that owned a number of assets in a dense metropolitan area, including parking lots and office buildings. Relative to the need for housing, putting those assets into development for multifamily housing would both have a higher ROI for the state and solve a real need for residents in that community.

Lucia Rahilly: What are some common misperceptions people have about affordable housing or about densifying their neighborhood?

JP Julien: There are a couple. First, folks think it's not their problem; it's not an issue they really want to deal with. The truth is that one in three American households were housing-cost burdened as of 2023. So, whether it's you or your neighbor to your left or your right, this is an everyday challenge that impacts families across our country in every kind of community you can think of.

The second is the idea that affordable housing is just not worth it. So, even if I agree that it's a problem, I don't really see the value in the long term. But again, there is an enormous economic and household benefit in solving this problem—to the tune of \$2 trillion over the next decade and as a fundamental lever to ensure American families can achieve their full potential.

Creative solutions to the crisis

Lucia Rahilly: The research covers a [range of solutions](#) to help alleviate the housing crisis. What's another you'd highlight?

JP Julien: The one that really stood out to me was off-site construction: the idea that you produce components off-site and then assemble them on-site, as opposed to doing everything on the site where housing is built.

Lucia Rahilly: Is that prefab?

JP Julien: There are elements of prefab techniques, like modular, in off-site construction. Modular in particular can be 20 to 50 percent faster in terms of delivery of units, 20 percent cheaper, and more energy efficient. At the same time, off-site construction as a whole represents somewhere between 3 and 4 percent of residential modular construction in the US today. So, one of the things we looked at was—we know this solution works, but why does it struggle to scale?

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degree, there is alignment that more housing is probably better.’

One of the underlying factors is state and local building codes. Today, if I build using modular techniques, I need to comply with state and local building codes that differ across state lines and sometimes even within a state. That lack of uniformity increases the complexity of what it takes to deliver. It results in delays and reduces the incentive to develop economies of scale, which would reduce the cost of production per unit.

We chatted with some off-site builders, and what we heard was, “I’ve cracked this in one state, and I know my technology works. I have real proof points and, in some cases, even investors who would be excited about me doing this in other states. But this seemingly small administrative complexity will cause a ton of challenges, so we’ve decided not to scale across state lines.” That’s where innovation is less about new dollars being invested and more about administrative tweaks that could be a huge unlock for the problem we’re trying to solve.

Lucia Rahilly: You mentioned there’s insufficient capital being invested in affordable housing, given the perception of a lower short-term return. Are you seeing any kind of innovative models, like public–private partnerships, that show more promise in enabling scale in affordable housing?

JP Julien: We are. One is helping financial institutions that need to be compliant with the Community Reinvestment Act, or CRA—essentially, making it easier for them to invest in affordable-housing projects. A lot of CRA dollars go to mortgages and small business loans. A smaller amount goes to multifamily affordable housing, particularly for rental purposes.

One small tweak here is, how do you develop preassembled portfolios of CRA-compliant, multifamily, affordable-housing investments that make it easier for smaller, less well-resourced financial institutions to find affordable-housing deals? And then offer those in packaged, atscale ways. Organizations like Community Capital Management are doing elements of this today that we could envision being further scaled.

‘Whether it’s you or your neighbor to your left or your right, this is an everyday challenge that impacts families across our country in every kind of community you can think of.’

Lucia Rahilly: Some of the solutions we’ve talked about feel like public sector solutions: zoning reform, for example. Is there a role for private sector leaders in addressing housing affordability?

JP Julien: There’s a huge role for the private sector. First, how and where are these leaders investing their capital? Whether that’s their endowment, their corporate treasury, or their overall

portfolio, allocating more of that underlying resource to affordable housing not only provides real risk-adjusted returns but also unlocks incredible benefits, including for their employees.

Second, as we talked about when we touched on zoning, your voice and your platform matter. When zoning reform works well, it's often both because residents agree it's a good thing and local business leaders advocate for what it could mean for that community. Leaders can think about leveraging their voice to champion this issue, both as good neighbors in the places where organizations are housed but also for the benefit of their employees.

What's at stake

Lucia Rahilly: What are the potential risks of not addressing this housing shortfall for the future, both economically and socially?

JP Julien: I think the risks are really pronounced. On one end, American families are working incredibly hard, doing everything they can to get ahead, supporting their families with everything they can muster, and still being forced to cough up 30 and 50 percent of their paychecks just to put a roof over their heads.

Our economic and social fabric relies on the belief that if you work hard and do your best, that effort will be rewarded—that you can save for your family's future, put away money for your kids, own a home. But this reality has been shifting for decades. Our housing crisis is showing how challenging that promise is becoming for so many families. The big risk is that by not addressing this issue, we see muted economic potential, we see economic mobility continue to be a challenge for millions of families, and we also renege on our promise as a country. I think that's a little of what's in the balance here in terms of risk.

Lucia Rahilly: So, we're confronting a crisis that is only growing more pervasive and more urgent. We also have a situation where state and local governments are busy taking on a lot. Budgets also don't seem to be expanding rapidly. What do you think is realistic in terms of what's achievable in the next, say, three to five years that could mitigate some of the effects of this housing shortfall? How optimistic are you?

JP Julien: I am a shameless optimist. I think we can solve hard problems, particularly hard problems that affect every state and every kind of community. There are things we can do to fundamentally change the trajectory of our housing shortfall. I am bullish on the idea that because it is so cross-cutting and ever-present, there's real willingness to solve the issue.

Second, not all these changes require capital. For many of the changes we talked about, whether public-private partnerships or reimagining zoning codes, there are relatively small administrative tweaks that could unlock a ton of benefit without requiring new investment. That's a bit of why I continue to be bullish.

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