Housing Prices: The Good, the Bad, and a Solution

**The Good**

Normally consumers like it when the prices of things they like to buy go down in price. Shelter is a necessity, so falling home prices make homes more affordable for people. This is great news to first time home buyers, or those who are looking to upsize their current house. Home ownership rates in the US lag those in Canada, so now is the time for people to join the ranks of the home owning population.

It’s a great time for home buyers to build equity in their houses. If they buy a house now, home prices are more likely to go up than down over the next five years. This increase in home prices will aid in people’s ability to save for retirement. Ever ask a financial advisor how to make money? Buy low, sell high. Housing prices sure are lower than they were a couple years ago. The average US home has become 28% cheaper.

Cheaper housing should mean that fewer people need to take advantage of public housing offered by the government. To qualify for public housing now, a family of four in Bowling Green, KY only needs to make $43,050 a year or less. With housing prices as low as they are, there really isn’t any need to hand out more tax money to pay for people’s housing who make $40,000 a year.

It is also a great time for people to buy that vacation home they have always wanted. Interest rates are historically low which makes it even easier to afford the payments on the newly lower priced condos. We wouldn’t have mass hysteria if the price of HD TV’s fell by 28%. In fact, most people, even if they owned one, would be happy with the price decrease.

**The Bad**

Over the past few years many Americans saw their homes as their chief mode of savings for retirement. They mistook the housing bubble for a real increase in their retirement savings and increased current consumption accordingly. Woops. As prices fell back to reality, many Americans found that they had now under saved for retirement. Savers should not save all of their eggs in one basket when they don’t have control of the basket. Future savers should use this experience to learn to diversify their savings.

Another problem faced by many Americans is that they took advantage of low interest rates and easy lending practices to buy houses with little or no money down. Let’s do the math. If you put 5% down on a house and that house loses 28% of its value, then it is a lot cheaper to walk away from the underwater mortgage than to pay it off.

Some of the US defaulters are doing so because they lost their jobs without sufficient rainy day funds. Some are strategically defaulting so that they don’t owe more on their house than it is worth. In this way they can take advantage of buying a new home at the newer low prices. There were also those who were just speculating on housing prices buying homes with the hope that their prices would go up. Here at Capitalism Today, we do not lose sleep when speculators make or lose money.

Mass defaulting on home loans has put a strain on many bank balance sheets. Banks are left with homes that can’t be sold for enough money to recoup the loan the banks made on the home. This is actually good news for well run banks who can now buy out more poorly run banks, but it is bad news for the shareholders of banks that made many bad real estate loans or bought asset backed securities. What these banks want is an increase in home prices to improve their balance sheets.

Another problem with an increase in foreclosures is that people who need to move to take advantage of new job opportunities are finding it to be more difficult to sell their existing homes. This may cause a reduction in labor force mobility and help to keep the unemployment rate artificially high.

**A Solution**

A solution presupposes that a problem exists. Are falling home prices a problem for some? Yes, but they are a benefit for others. In this light, it really isn’t appropriate for the federal government to intervene in markets to try to “fix” housing prices. It’s more efficient to let markets determine prices than have governments assign arbitrary prices to products.

That being said, if the federal government is looking to boost housing prices, the most market friendly reform would be to loosen legal immigration rules. The more people who are in the US that can legally buy homes, the greater the demand will be for US homes, which, in turn, will cause the price of existing houses to increase. The housing collapse of the 1920’s was in part caused by new regulations restricting immigration into the US. A reversal of these policies will lead to a turnaround in US housing prices.

If people in other countries want to become a US citizen, then let them put 20% down on a house and pass the citizenship test. That and a criminal background check should earn them US citizenship, and the rest of us get appreciating home values.

As is often the case, solutions to problems are usually economically straightforward, but politically problematic. The politically popular thing apparently is to bail out banks who made bad loans, and consumers who took on too much debt with taxpayer money. Economically, however, that just exacerbates the problem.

In the end, if you want housing prices to increase, (and you may not), then you can either wait until consumers save enough to start putting 20% down on their homes, allow more immigration of home buyers, or learn to deal with lower home prices. Short sighted government bailouts and ever more generous public housing subsidies only work to depress home prices. While stimulating housing prices is dubious government policy, it would be nice for government policy to actually match up with their publicly stated goals. Of course, that may be asking too much of politicians.