Tax Changes and the Housing Market

Tax effects take time to materialize in data.
"Virtually all serious economists expect the impact will not be felt immediately. Economic data is produced on a lag. And it will be difficult to prove that gains were linked to the tax bill. We won't get to that level of specificity until years from now." [1] --Scott Greenberg, a senior analyst for the Tax Foundation

NAR is forecasting home prices to grow 5.1 percent in 2018 and 3.8 percent in 2019, lower than they would have been without tax reform, but stronger than before inventory shortages took hold this spring.

Steady home price growth reflects long-term trends.
In particular, the historically low level of inventory, measured in the first quarter at 4.0 months to exhaust the current supply (or roughly half what is considered a neutral market) is the lowest level since NAR began measuring it in 1999. This shortage reflects a construction deficit of 3.5 to 4 million single-family homes that have not been built since the crisis, which will maintain pressure on prices until construction catches up. It could take a decade for construction to catch up to demand.

Home prices typically lag changes in home sales.
While some surveys show plans to buy a home may be up, home sales are down 1.7 percent in the first quarter of 2018 compared to the same period in 2017. The Northeast and West were down 8.1 percent and 2.2 percent over this period, respectively, along with the Midwest, which fell 1.8 percent. The South was able to expand 0.7 percent. Higher mortgage rates, housing shortages, and tax impacts likely contributed to the decline.

While millions of households received a boost to their wages via lower income taxes this spring, most homeowners and homebuyers will not get clarity on the loss of tax benefits from housing until they file their 2018 tax return in the spring of 2019.

Home price growth and inflation will push more homeowners and home buyers above the $10,000 SALT and $750,000 MID caps over time. As mortgage rates rise in the coming decade, the weight of these caps and lost or limited mortgage interest deduction will grow on most home owners and buyers like the AMT.

Married home-owning couples who choose to itemize face a new marriage tax penalty.
They receive the same $10,000 maximum SALT deduction as single homeowners despite earning on average nearly 50 percent more and owning homes twice as expensive as singles. This disparity is more apparent as home size and prices rise with family size.

Builders and investors respond to market signals.
The new tax law lowered tax benefits for buying and owning a home while encouraging the ownership of rental property. This effectively raises taxes on home ownership and increases the marginal cost of owning relative to renting, creating incentives for builders and investors to put their money in rental stock rather than owner-occupied stock. This trend will further exacerbate owner-occupied housing shortages.

The current homeownership rate of 64.2 percent in the first quarter languishes near its 50-year low.
If the homeownership rate were at its long-term average of 65.5 percent, nearly two million additional American households would own their own home. Reducing the tax benefits of ownership for homeowners and aspiring homeowners adds to the headwinds of rising mortgage rates and supply shortages that buffet attempts to normalize homeownership.

[1] http://www.politifact.com/truth-o-meter/article/2018/feb/01/how-quickly-will-new-tax-law-affect-economy/

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