THE MYTH OF HOMEOWNERSHIP

Homeownership promises more than it delivers. Americans purchase homes for perceived financial security and social benefits, while politicians push homeownership for imagined economic growth. Such claims are traded like stock tips around water coolers and repeated by "experts" paid by the real estate and homebuilding industries. But they are merely myths, widely held but false. Here are some of the biggest whoppers.

Homeownership is a good investment.

According to housing guru Robert Shiller, from 1950 to 2000, annualized returns to housing averaged less than 0.5 percent after adjusting for inflation. Returns were even lower over a longer horizon, with real prices growing 0.4 percent per year from 1890 to 2004. Relative to other investments, owner-occupied housing has grossly underperformed. Between 1926 and 2009, compounded annual returns for small stocks (11.9 percent), large stocks (9.8), long-term government bonds (5.4), and Treasury bills (3.7) far outpaced housing returns.

Owning a home is not the path to prosperity. At best, homeownership amounts to a decent savings account, but even then it is ineffective. Policies like the mortgage interest deduction (MID) encourage taxpayers to finance homes with debt, and result in leveraged ownership not true ownership. Between 1950 and 2010, the percentage of home equity plunged from 80 percent to 38.5 percent. In the words of one commentator, "the cold, unsentimental fact about the American dream is that Americans never really owned it in the first place."

Homeownership creates positive social benefits.

The housing industry likes to say that homeowners enjoy better lives than renters. It touts studies correlating homeownership with higher rates of civic participation, beneficial effects on children's wellbeing and behavior, and lower rates of crime.

But no study has identified a causal connection between homeownership and what economists call "social capital." Children of homeowners might exhibit lower rates of truancy than children of renters, but that doesn't mean renting will land your kid in juvenile hall or that owning will get her into Harvard. In fact, studies that isolate causal influences of homeownership on social capital find that the purported benefits disappear and even become negative.

Housing subsidies lower the cost of homeownership.

Current housing policies distort the allocation of financial capital by altering the decision to pay for homeownership with debt over cash or other assets. Thanks particularly to the MID, mortgage indebtedness soared in the decade preceding the housing collapse, rising as a percentage of GDP from 47 percent in 1995 to 81 percent by 2007.

Subsidized mortgage debt encourages homebuyers to consume bigger, costlier homes. Yet artificially boosting the cost of housing helps no one. Higher prices prevent millions of potential homebuyers from entering the market. And while current homeowners may prefer inflated prices for maximizing gain upon sale, any perceived benefit is illusory as sellers become buyers in the same over-heated market.

Housing subsidies help the economy.

Housing subsidies distort the decision over where to invest as much as how to invest. By lowering the cost of owner-occupied housing, subsidies contribute to overinvestment in residential real estate. “Don’t build a factory, build a mansion,” economist Kevin Hassett has said of the MID’s influence on capital investment. Indeed, while the tax rate on corporate investment exceeds 30 percent, housing enjoys a rate near zero.

The distortions caused by tax subsidies for housing may account for half of all misallocated capital in the economy, shrinking GDP by 10 percent. They also contribute to labor immobility, which raises unemployment. No wonder nearly every economist believes “the most sure-fire way to improve the competitiveness of the American economy is to repeal the mortgage interest deduction.”

Housing subsidies help middle-class families.

Subsidies for homeownership accrue disproportionately to upper-income households. Only 3 percent of taxpayers report income over $200,000, but they enjoy 35 percent of the MID’s largesse, while the 75 percent of all taxpayers earning less than $75,000 receive just 11 percent. In fact, the MID delivers ten times the savings for households with income over $250,000 compared to those with income between $40,000 and $75,000.

The disparity in benefits exists because taxpayers receive them only if they itemize deductions. But just one-third of taxpayers itemize, while two-thirds take the standard deduction (and thus receive no benefits). Even among itemizers, high-income households receive larger benefits, because the value of the subsidy rises as taxable income increases.

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There are good reasons to buy a house. But none of them involve attaining financial security, admission to elite colleges, a stronger economy, lower taxes, or the American Dream.

Dennis J. Ventry, Jr. is a professor at UC Davis School of Law specializing in tax and legal ethics, and author of “The Fake Third Rail of Tax Reform” and “The Accidental Deduction.”