Statement of Dr. Kenneth Rosen
Chair of the Fisher Center for Real Estate and Urban Economics at the Haas School of Business, University of California, Berkeley
For
Submission to the Record

U.S. House
Committee on Small Business

October 7, 2009

Statement of Dr. Kenneth Rosen,
Haas School of Business, University of California, Berkeley

Chairwoman Velazquez, Ranking Member Graves, and Members of the Committee, thank you for the opportunity to submit a statement to the Congressional Record regarding the first-time homebuyer tax credit.

My name is Dr. Kenneth Rosen and I am the Chair of the Fisher Center for Real Estate and Urban Economics at the Haas School of Business at the University of California, Berkeley. I am also the Chairman of the Rosen Consulting Group, and I have spent my career focused on housing economics, and in fact, originated the premise for the 1974-1975 homebuyer tax credit.

The Fix Housing First Coalition retained the Rosen Consulting Group to evaluate the effectiveness of the first-time homebuyer tax credit in stimulating consumer demand and reducing the supply of home available for sale.

Therefore, I submit testimony today based upon the results of that study, released the end of September entitled "*Examining the First-Time Homebuyer Tax Credit*." The study provides empirical analysis on how the tax credit is reducing housing inventories and stabilizing home prices.

For your reference I am attaching the executive summary of the study to this statement.

As you in Congress evaluate the success of the American Recovery and Reinvestment Act of 2009, the study makes clear that the first-time homebuyer tax credit is an unparalleled standout from that package, with stimulative effects that go far beyond the single purchase of a home.

Beyond quantifying the strong success of this credit, the study clearly demonstrates the urgency of passing a temporary extension and expansion of the credit to prevent a halting of the housing recovery and a slowing of the economy's new-found momentum.

To best understand the study's findings, let us look again at the housing problem.

The housing sector is currently locked in a self-reinforcing cycle of rising foreclosures and falling prices.

This cycle is the direct result of a surplus in the supply of homes for sale relative to consumer demand. A combination of programs aimed at reducing foreclosures and stimulating consumer demand is needed to stabilize this very important sector of the economy.

In recent weeks, the housing market has shown a modest increase in sales volume and prices appear to have stabilized, albeit at low levels.

My report demonstrated that these improvements are primarily attributable to the effectiveness of the first-time homebuyer tax credit in reducing excess inventory.

The study found that the first-time homebuyer tax credit has served to stimulate demand for homes, particularly among low and middle-income families. It is proving effective in reducing the supply of homes, as the credit has been the primary cause – buffeted by increased affordability – of the return of buyers to the housing market over the past several months.

The inventory of homes for sale has been reduced as a result of the tax credit, particularly at the lower end of the pricing spectrum.

For homes priced at less than $300,000, the supply has decreased by 25.9% versus a year ago; and for homes priced within the $300,000 to $500,000 range, the supply has dropped by 18.4%. These numbers demonstrate that the credit is particularly effective at bringing working families into the market.

When the credit was passed as part of the stimulus package, many were concerned that it might spur speculative new home construction, rather than inspiring purchasers to acquire from the existing supply.

However, the study illustrates that housing starts continue to remain very low, with the annualized second quarter starts totaling 423,000 homes, approximately 60% lower than the long-term average, and the second-lowest quarterly figure on record.

Notwithstanding the encouraging indicators within the housing market, the study also notes that the sector remains at historically depressed levels and, most importantly, faces continuing challenges from rising unemployment, the threat of further price depreciation and elevated foreclosures that will persist for the next 12 to 18 months.

For example, as many foreclosures become lender-owned, they add to the supply of available homes. If the credit is allowed to expire, it is likely that lender-owned properties will quickly increase in available supply, at the same time buyer demand significantly retracts.

Without a temporary extension of the credit, it is very probable that the housing market will fall back to levels of the fourth-quarter of 2008, when the overall economy imploded.

Beyond simply extending the tax credit, an expansion of the credit would spur an increase similar to what has occurred in the lower end of the market, by motivating buyers in the “trade-up market” to purchase a higher-priced primary home.

Expanding the income limits to $125,000 for individuals and $250,000 for a married couple would also enable more households to take advantage of the credit and spur additional demand.

Of the multitude of provisions in the stimulus package, it is clear that the tax credit stands out as a stellar success.

It’s efficient in that funding goes directly to taxpayers; it’s leveragable because it triggers large amounts of economic activity; and it is achieving its specific goal to begin to reduce inventories and stabilize home prices.

In short, it meets President Obama's benchmark for stimulus initiatives – it is temporary, targeted, and timely.

Right now housing is one of the only components driving our economic recovery, and the tax credit is largely responsible for housing's momentum.

But in less than two months, the tax credit's expiration would likely cause a relapse in the housing market that the nation's fragile economy could sorely afford.

A recovery in the residential market has led the nation out of recession in nearly every economic recovery of the past 40 years.

Housing is an unusually dynamic industry with home purchases stimulating activity beyond the single transaction to extend into retail, manufacturing, and even provide fiscal benefits to help local governments get back on healthy financial footing.

The first-time homebuyer tax credit has proven to be an effective tool in stimulating demand and reducing supply. Given current conditions in the housing market, this program should be temporarily extended and expanded.

Thank you for this opportunity.

###