

Buying a Home in the Washington DC Metro Area is a Good Long-Term Financial Investment

By Lisa A. Fowler, PhD and John McClain

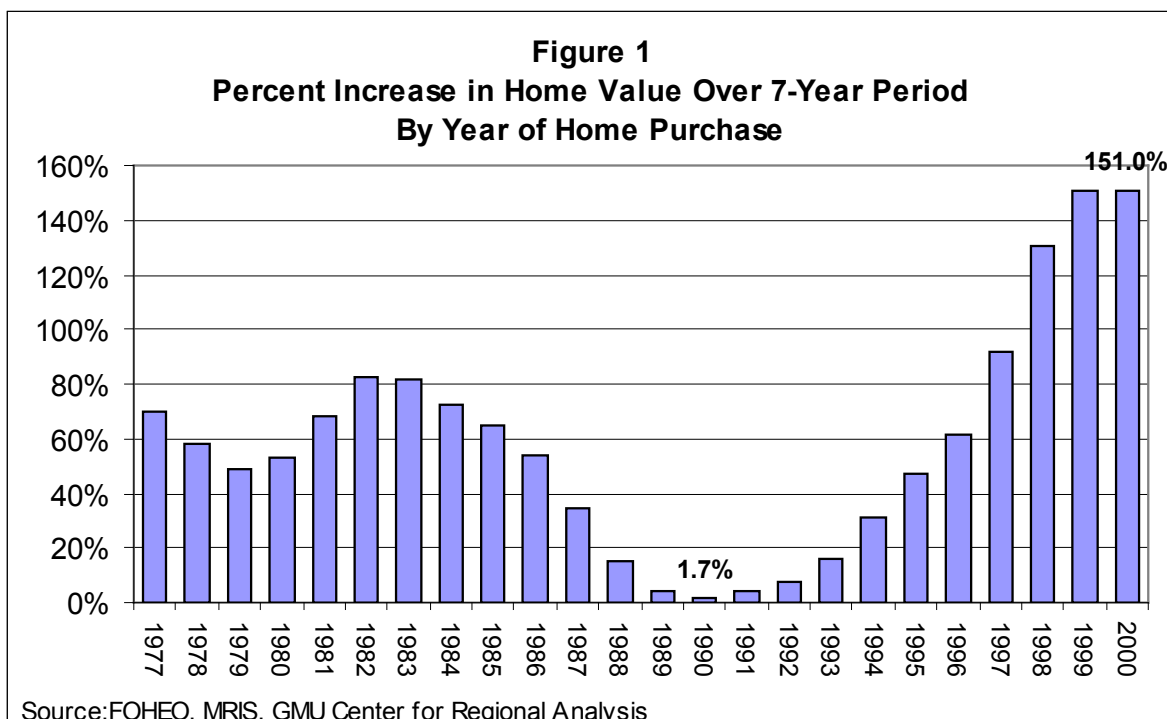
Why do people buy a home? People often buy a home to feel connected to a community, to have freedom over their living space, to raise a family or to put down roots. Many people anticipate that their home also will be a good financial investment. As an investment, housing has performed remarkably well over time. Even in slower markets, buying a home is sure to provide a positive financial return over time. Over the past 30 years, investment in housing in the Washington DC metropolitan area has provided a better return than investing in the stock market.

Housing as a Valuable Asset

The average homeowner in the Washington DC metropolitan area has lived in their home for seven years. If people buy homes to live in, rather than to flip for a quick profit, there is little chance of losing money. Over the past 30 years, there has been no seven-year period where the average home price in the metropolitan area has declined. Home prices have grown, on average, nearly eight percent annually or 54 percent over a seven-year period during the past three decades. People who bought homes in the early 1990s in the Washington DC metropolitan area—and lived in them the average tenure of seven years—experienced the lowest growth in home values (Figure 1). Home prices in the metro area grew 1.7 percent between 1990 and 1997.

At the same time, however, the metro area economy was losing jobs. The region was particularly hard hit in 1991 and 1992 when 61,000 jobs were lost, primarily due to the national recession in those years.

The value of homes quickly rebounded as the region's economy improved. Home price appreciation increased steadily over the late 1990s. As we all know, home values have increased spectacularly over recent years. A home bought in 2000 was worth 151 percent more than its purchase price seven years later.



Housing Providing a Great Return on Investment

Another way to look at the financial benefits of buying a home is to examine the return on investment for a homebuyer. If a \$200,000 home increase in value over seven years to \$300,000, the increase in value is \$100,000. If the homebuyer put down 20 percent at the time of purchase (\$40,000), the appreciate results in a return on investment of \$60,000, or a 50 percent return on his investment. (The return on the investment in the home is the increase in the value of the home, minus the down payment amount.)

Figure 2 shows the seven-year return on investments in housing in the Washington DC region and investments in the NASDAQ stock exchange over the past 30 years. Assuming an individual invested 20 percent of the average sale price of a home in the Washington DC metropolitan area in the NASDAQ, Figure 2 shows that he usually would experience a lower rate of return on his investment compared with buying a home.

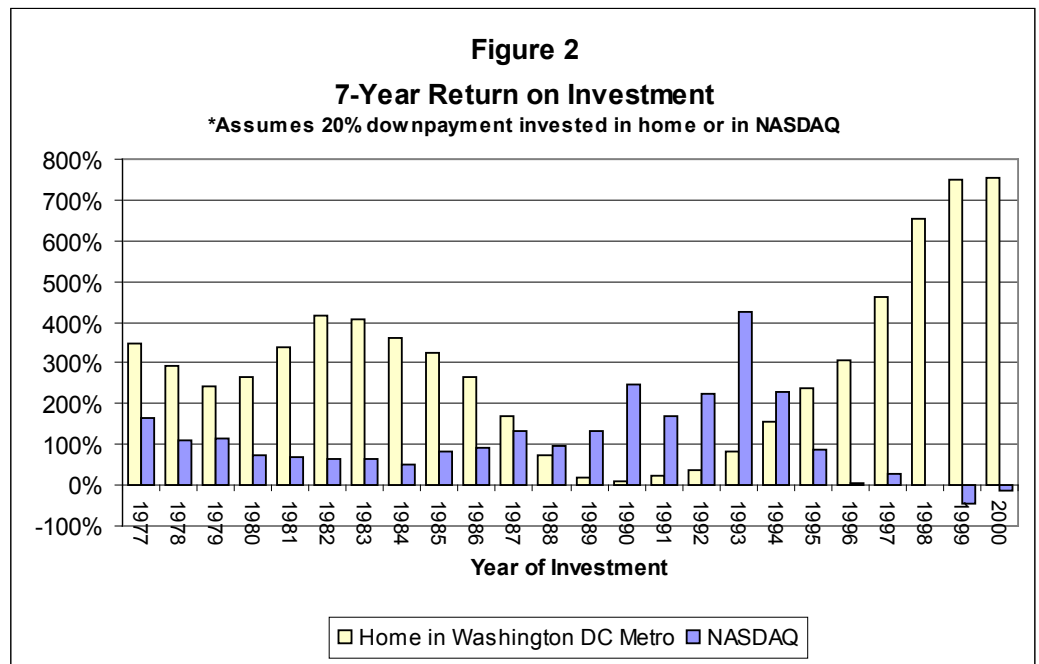
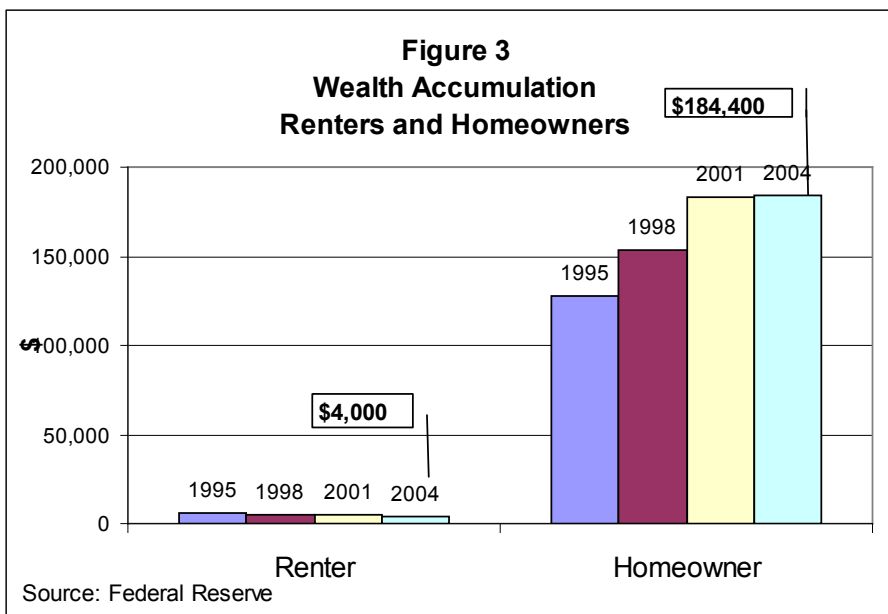


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In some periods, the stock market provided better returns than housing. In particular, in the early 1990s, one would have been better off financially investing in the stock market than in the metro area housing market. However, in only seven years over the last thirty years was an investment in the NASDAQ superior to investment in the Washington DC area housing market, and over the 22 years the average seven year change was 292% for investment in a house and 108% for investment in the NASDAQ.

Housing Wealth

Perhaps the best financial rationale for buying a home is that it provides people with an unrivaled opportunity for wealth creation. According to the Federal Reserve, homeowners accumulate 45 times more personal wealth than do renters (Figure 3.)



In 2004, the wealth of an average homeowner was more than \$184,000, compared with \$4,000 for the average renting household.

In the end, buying a home is about more than a financial investment. Potential buyers who plan to live in a home for more than one or two years, and who want to take advantage of continuing low interest rates, there is no reason not to buy a home now in the Washington DC metropolitan area. Based on a review of 30 years of data, the fear of failing to realize a return on investment in a home in the region is unfounded.