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“Is There a Bubble in the Housing Market?”

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This paper looks for evidence of a bubble in U.S. housing prices. It analyzes quarterly state-level data over 1985-2002, focusing on the relationship between home prices and selected fundamental variables. Income per capita alone largely explains price changes in all but eight states; in the latter, large price movements are observed unrelated to the fundamentals. Results from a new survey of recent homebuyers in the Los Angeles, San Francisco, Boston, and Milwaukee metropolitan areas are reported. This survey replicates an almost identical 1988 survey and finds, as before, that buyers in most of these markets perceive little risk in their housing investment, have unrealistic expectations about future price increases, and hold economically implausible beliefs about home price behavior—findings consistent with a bubble. Prices in such markets could stall or decline, but only if such declines are simultaneous or spread to other markets are significant effects on the national economy likely.