Fiscal Cliff – What's At Stack for Real Estate December 14, 2012

The "fiscal cliff" has quickly become a commonly used term, but exactly what it means isn't all that clear, especially for real estate. At it's most basic level, it refers to sweeping tax cuts enacted a decade ago that will expire at year's end, so tax rates will automatically rise to where they were before, while at the same time automatic spending cuts—the sequestration enacted when the government's borrowing limit was raised a year ago–will take effect. Thus, the economy faces a two-pronged hit: taxes going up while federal fiscal spending goes down.

If Congress does nothing, that double hit would mean a negative economic impact of about $650 billion, enough to shrink the economy by 4 percent and push the country back into recession, says NAR Chief Economist Lawrence Yun.

For real estate, that has the potential to derail the recovery that's been slowly taking hold. Foreclosures would rise, home values would drop, hurting households but also hurting FHA, which could get hit with another wave of bad loans. That could put FHA into financial trouble.

Against this background, the federal government will be looking at a lot of options for averting the cliff while also lowering the federal budget deficit for the long-term. That puts the mortgage interest deduction in the spotlight. But is it a good idea to make changes to that tax provision?

Without a doubt, changing the rules of the game on MID now would mean a tremendous hit on real estate markets and household finances, and it could deal a blow to the broader economy, says Yun.

He and NAR economist Danielle Hale look at the different pieces in play under the fiscal cliff debate and also the economic impact of changing MID in the **9-minute video** above. The information is intended to be helpful as you try to put the fiscal cliff conversation into perspective.