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The Psychology of Buying and Selling a House

How our emotions influence the homes we choose and the prices we pay

By **MATTHEW KASSEL**

It's a fact of life: Homes come with far more emotional weight than any other investment we make.

A home is a refuge from the world, a place to raise a family and, for some people, an investment they hope will bring them a good chunk of money down the road. We fall in love with houses in a way that we never fall in love with a portfolio of stocks and bonds.

All too often, though, we don't realize that how we feel about homes blinds us when it comes time to buy or sell. We let our emotions blind us to cold facts about the market or the realities of ownership. Or we prioritize one set of emotional needs over others that are just are strong but may not be evident at first. And ignoring them can lead us to make bad financial decisions that can affect us for decades to come.

For instance, people might focus on their desire for a house that's a certain size or style, but ignore the fact that they want to spend as much time as possible with family. So they might buy a "perfect" house that requires them to make a long daily commute to work and keeps them away from home for two extra hours each day.

The home-selling side of the equation brings its own set of thorny issues. Homeowners often have an overly rosy view of their home and expect it to increase in value far beyond reasonable expectations. And when they put it on the market, they often stubbornly cling to their asking price—even if it means leaving it up for sale far longer than they planned, and risking the possibility of not selling it at all.

Here's a closer look at some psychological missteps that buyers and sellers often make as they wade into the housing market.

Ignoring the big picture

Home buyers are always on the lookout for features—like a longer driveway or bigger backyard—that will make them happier with their home. But people don't realize that those changes may not make them happier with their life as a whole.

"When people move to a better housing, they think they will be a lot happier overall," saysShige Oishi, a co-author of a 2010 study on the subject in Social Indicators Research. "When they actually move, however, their overall happiness does not often change because there are many trade-offs in moving."

One of the biggest trade-offs is commuting. Many move to live in a bigger house, but that bigger house is often farther away from work—so that means more commuting, which tends to add stress and detract from overall happiness. A 2008 study in the Scandinavian Journal of Economics shows that people who had longer commutes reported "lower subjective well-being" than those with shorter commutes. "If you're moving to a place far away from your friends, but it has nicer stuff, it's not a great deal for your happiness," saysElizabeth Dunn, a psychology professor at the University of British Columbia.

In another study in the Personality and Social Psychology Bulletin, Ms. Dunn and her co-authors explored the matter of expectations vs. reality in another way—by looking at Harvard undergraduates who were randomly assigned to different dormitories. The study showed that first-year students incorrectly predicted what would bring them the most satisfaction from their dorms—physical features like location on campus, the attractiveness of the residence, room size and desirability of the dining hall and facilities.

In the initial survey, the students put no weight on social features, such as relationships with roommates and a sense of community in the residence. But when the researchers checked back in with the students after they'd been living in their dorms, the only thing that appeared to matter for their happiness was the quality of the social factors.

"It's so easy to get caught up in comparing the physical features of the places you're looking at," says Ms. Dunn, "but you should really stop to consider how the places you're considering will shape your social relationships."

Overlooking big expenses

People who are buying homes tend to compartmentalize their expenses and not add up the total cost of everything needed to fix up and furnish the house, says Alex Tabarrok, a professor of economics at George Mason University. That can lead them to make poor choices about how much to pay for a home. For instance, they may overspend on a down payment for the house itself and leave themselves without enough money to buy the sort of decorations or furniture that they want. “When you’re getting a house, think about furnishing it at the same time,” says Mr. Tabarrok.

Weighing buying vs. renting

The biggest budgeting concern is, of course, whether you should buy a house at all. Research shows there are psychological benefits to taking the plunge—but also to opting out.

Buying a house can give people a psychological boost by making them feel like they’ve “arrived” and are part of the American ideal. Homeowners also may feel as though they have more control over their lives since they’re not dependent on the whims of a fickle landlord.

But while those factors may lead people into buying a house, there are other negative elements that homeowners don’t discover until after they’ve taken the plunge.

Research, for instance, has shown that home ownership can cause undue stress. The amount of work necessary to maintain a home—such as decorating, or mowing the lawn every weekend—may be too much for some people. Others may be overwhelmed by the financial aspect of ownership, such as being tied to a big monthly mortgage, or keeping up with repairs and other unforeseen costs.

Expecting a big return

When it comes to selling a home, most people aren't in for a huge payday. Yet many are overly optimistic in their home-price expectations, according to Robert J. Shiller.

Dr. Shiller, a professor of economics at Yale University, co-wrote a paper, updated in 2014, that looked at the ways recent home buyers around the country think about the future values of their properties.

Using questionnaire surveys, Mr. Shiller and his co-authors found, among other things, that home buyers have extremely high long-term price expectations. That can lead people to buy homes that aren’t a good fit in terms of location or social scene just because they seem like good investments. Or they may stake their plans—such as retirement—on a certain return and find themselves scrambling when they come up short. On a larger scale, this over-optimism can lead to speculative booms that warp the market.

While it isn’t entirely clear why homeowners are usually so cheerful about the future, the researchers postulate it may result from the “money illusion”—a failure to take inflation into account.

“Imagine that your grandmother dies, and you’re managing her estate,” Mr. Shiller says. “Her house is worth $30,000 now, and you look at what she paid—$5,000. You think, ‘Wow, that’s a lot.’ Now why does it seem so big? Because you’re not reflecting that all prices went up sixfold” and you’re basically not making a profit after taking inflation into account.

Not wanting to come up short

People have many reasons for selling their homes, and for setting the prices they do. But research has found that the most powerful emotional drive at work in a sale is loss aversion—not wanting to sell a home for less than what you paid for it.

In a study in The Quarterly Journal of Economics, researchers found that homeowners latch on to the price they paid for their home with the hope that they can get more when they put it on the market. But that isn’t the soundest idea, says Christopher Mayer, a co-author of the study and a professor of real estate and economics at Columbia Business School, especially if your house has depreciated in value. It’s a fallacy to assume that you’ll be able to recoup losses you’ve already incurred. The current market price has nothing to do with how much a person actually paid for it.

There is a nuance here, though. People who stubbornly stick to an asking price above market value risk not selling their house at all. But sometimes they are rewarded.

Mr. Mayer and a co-author analyzed housing data from downtown Boston in the 1990s, culled from a boom-bust cycle. Condominium owners who put their houses up for sale above the market rate—though still below what they paid for them—sold their homes for more than expected, even as their properties lingered on the market for longer than usual.