Profitability of Texas Homes

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How profitable are Texas houses as an investment? An ongoing research project at the Real Estate Center at Texas A&M University found that Texas homes are more profitable than the national average, and significant variations in profitability exist across the state's metropolitan housing markets.

The Takeaway

Texas homes are profitable investments, with yields exceeding the national average for homes in most metro areas when profitability is measured in terms of average yield. Average yields on Texas homes exceeded yields for McDonald's Corporation, Home Depot and Lowe's in the 2009–13 period.

Home as Investment

Owner-occupied homes are both consumer goods and investment goods. Once a house is built, it generates streams of current and future benefits in the form of rental incomes and streams of costs in the form of maintenance, insurance and taxes. From an investment perspective, homes have to compete with alternative investments such as bonds and stocks for profitability measured in terms of yield or rate of return on investment. Investors in asset markets compare yield returns on different assets and channel their investing funds to assets generating the best returns. Over time, yields or rates of return on various investment goods in asset markets tend to converge to their long-term equilibrium values.

Measuring Profitability

Several methods exist for measuring the profitability of housing investments. This research project used net rental yield because financial data for Texas homes was readily available.

For stocks, dividend or earnings yield is computed by dividing total dividends or earnings paid during a period by the stock price. In real estate economics, gross rental yield and net rental yield are used to measure the profitability of rental properties as investments. Gross rental yield is simply annual rent as a percentage of the property price. For instance, if annual rent for a house is $24,000 and the house price is $200,000, the gross rental yield is 12 percent. This is the return on investment before the homeowner's costs.

Net rental yield on homes is computed by dividing net profit from renting a house by the house price. Net profit is equal to annual gross rent minus annual housing costs including property tax, insurance, maintenance costs and management fees. If annual operating costs for our example total $18,000, annual net rent is $6,000, resulting in a net rental yield of 3 percent. Net rental yields are also called capitalization rates or cap rates.

Computing Net Rental Yields

Data for computing net rental yields on Texas homes were collected from the 2009–13 datasets of the U.S. Census Bureau's American Housing Survey. The data are five-year averages of median gross rents, median homeowner costs, and median home values for 2009–13. Both the rent and housing cost data in the survey include costs of utilities. When housing costs are deducted from rents, the resultant net profit or net rent figures are net of the costs of utilities.

Table 1 shows Texas metropolitan areas ranked by median annual gross rent. Austin-Round Rock had the highest gross rent from 2009 to 2013 followed by Midland, Dallas-Fort Worth-Arlington, Houston-Sugar Land and Killeen-Temple. The median gross rents for these five Texas metro areas were higher than the statewide average. The first three metro areas had gross rents even higher than the national average. At the bottom of the table, Brownsville-Harlingen had the lowest gross median rent followed by McAllen-Edinburg-Mission, Texarkana and El Paso.

Homeowner costs are the second component for computing net rental yields. Table 2 presents Texas metropolitan areas ranked by homeowner costs (taxes, insurance and maintenance costs). Austin-Round Rock had the highest

Table 1. Texas Metro Areas Ranked by Median Annual Rents, 2009–13

Rank	Region	Gross Rent (Dollars)
1	Austin-Round Rock	11,856
2	Midland	11,316
3	Dallas-Fort Worth-Arlington	10,848
	United States	**10,848**
4	Houston-Sugar Land	10,728
5	Killeen-Temple	10,320
	Texas	**10,212**
6	San Antonio-New Braunfels	10,092
7	College Station-Bryan	10,068
8	Corpus Christi	9,996
9	Tyler	9,936
10	Odessa	9,468
11	Lubbock	9,360
12	Sherman-Denison	9,216
13	Waco	9,048
14	Abilene	8,964
15	Laredo	8,904
16	Victoria	8,820
17	Beaumont-Port Arthur	8,736
18	Longview	8,700
18	Amarillo	8,700
20	Wichita Falls	8,688
21	San Angelo	8,664
22	El Paso	8,640
23	Texarkana	8,364
24	McAllen-Edinburg-Mission	7,692
25	Brownsville-Harlingen	7,668

Source: U.S. Census Bureau

Table 2. Texas Metro Areas Ranked by Median Annual Homeowner Costs, 2009–13

Rank	Region	Homeowner Costs (Dollars)
1	Austin-Round Rock	7,200
2	Dallas-Fort Worth-Arlington	6,552
3	Houston-Sugar Land	6,372
4	Midland	5,844
5	College Station-Bryan	5,484
6	Victoria	5,448
	Texas	**5,424**
	United States	**5,424**
7	Corpus Christi	5,400
8	Sherman-Denison	5,364
9	Killeen-Temple	5,328
9	Laredo	5,328
11	Wichita Falls	5,292
12	Waco	5,256
13	Lubbock	5,196
13	San Antonio-New Braunfels	5,196
15	Tyler	5,124
16	Amarillo	4,932
17	Abilene	4,716
17	San Angelo	4,716
19	Odessa	4,596
20	Beaumont-Port Arthur	4,560
21	Texarkana	4,488
22	Longview	4,320
23	Brownsville-Harlingen	4,260
24	El Paso	4,164
25	McAllen-Edinburg-Mission	4,152

Source: U.S. Census Bureau

owner costs followed by Dallas-Fort Worth-Arlington, Houston-Sugar Land, Midland, College Station-Bryan and Victoria, all higher than the national and statewide averages. McAllen-Edinburg-Mission had the lowest owner costs followed by El Paso, Brownsville-Harlingen and Longview.

Deducting homeowner costs from gross rents for each Texas metropolitan area results in net rental income (Table 3). Midland had the highest net rent, even higher than the national average, followed by Killeen-Temple, San Antonio-New Braunfels, Odessa and Tyler. Victoria had the lowest net rental income followed by Wichita Falls, Brownsville-Harlingen and McAllen-Edinburg-Mission.

For computing net rental yields, net rental income for each metro area is compared with the median home value for the area. Texas metropolitan areas are ranked by the median value of owner-occupied homes in Table 4. Austin-Round Rock had the highest home prices, even higher than the national average, followed by Dallas-Fort Worth-Arlington, Midland, Houston-Sugar Land, College Station-Bryan and San Antonio-New Braunfels.

Dividing net rent for each region from Table 3 by the median home value for the region in Table 4 and multiplying the resultant number by 100 gives net rental yields (Table 5). The average net rental yield for Texas from 2009–13 was 3.71 percent, well above the 3.07 percent for the United States. Odessa had the highest net rental yield followed by Abilene, McAllen-Edinburg-Mission, Beaumont-Port Arthur and Brownsville-Harlingen. At the bottom of the rankings are Austin-Round Rock, Dallas-Fort Worth-Arlington, Victoria and Houston-Sugar Land.

Comparing median home values in Table 4 and net rents in Table 3 shows that the main reason for lower net rental yields in the metropolitan areas of Austin-Round Rock, Dallas-Fort Worth and Houston-Sugar Land is their higher home prices. For comparison, five-year average dividend yields for McDonald's Corporation, Home Depot and Lowe's were 3.30 percent, 2.2 percent and 1.7 percent, respectively.

Table 3. Texas Metro Areas Ranked by Median Annual Net Rent, 2009–13

Rank	Region	Net Rent (Dollars)
1	Midland	5,472
	United States	**5,424**
2	Killeen-Temple	4,992
3	San Antonio-New Braunfels	4,896
4	Odessa	4,872
5	Tyler	4,812
	Texas	**4,788**
6	Austin-Round Rock	4,656
7	Corpus Christi	4,596
8	College Station-Bryan	4,584
9	El Paso	4,476
10	Longview	4,380
11	Houston-Sugar Land	4,356
12	Dallas-Fort Worth-Arlington	4,296
13	Abilene	4,248
14	Beaumont-Port Arthur	4,176
15	Lubbock	4,164
16	San Angelo	3,948
17	Texarkana	3,876
18	Sherman-Denison	3,852
19	Waco	3,792
20	Amarillo	3,768
21	Laredo	3,576
22	McAllen-Edinburg-Mission	3,540
23	Brownsville-Harlingen	3,408
24	Wichita Falls	3,396
25	Victoria	3,372

Source: U.S. Census Bureau

Table 4. Texas Metro Areas Ranked by Median Value of Homes, 2009–13

Rank	Region	Median Value (Dollars)
1	Austin-Round Rock	192,000
	United States	**176,700**
2	Dallas-Fort Worth-Arlington	150,000
3	Midland	145,700
4	Houston-Sugar Land	141,400
5	College Station-Bryan	140,200
6	San Antonio-New Braunfels	131,100
	Texas	**128,900**
7	Tyler	120,800
8	Killeen-Temple	119,200
9	Amarillo	116,800
10	El Paso	111,400
11	Victoria	110,300
12	Laredo	108,800
13	Longview	108,000
14	Corpus Christi	107,700
15	Lubbock	106,800
16	Sherman-Denison	104,500
17	Waco	104,200
18	San Angelo	98,800
19	Beaumont-Port Arthur	95,200
20	Texarkana	95,100
21	Odessa	91,200
22	Wichita Falls	89,400
23	Abilene	89,000
24	Brownsville-Harlingen	78,300
25	McAllen-Edinburg-Mission	78,100

Source: U.S. Census Bureau

Table 5. Texas Metro Areas Ranked by Net Rental Yield, 2009–13

Rank	Region	Yield (Percent)
1	Odessa	5.34
2	Abilene	4.77
3	McAllen-Edinburg-Mission	4.53
4	Beaumont-Port Arthur	4.39
5	Brownsville-Harlingen	4.35
6	Corpus Christi	4.27
7	Killeen-Temple	4.19
8	Texarkana	4.08
9	Longview	4.06
10	El Paso	4.02
11	San Angelo	4.00
12	Tyler	3.98
13	Lubbock	3.90
14	Wichita Falls	3.80
15	Midland	3.76
16	San Antonio-New Braunfels	3.73
	Texas	**3.71**
17	Sherman-Denison	3.69
18	Waco	3.64
19	Laredo	3.29
20	College Station-Bryan	3.27
21	Amarillo	3.23
22	Houston-Sugar Land	3.08
	United States	**3.07**
23	Victoria	3.06
24	Dallas-Fort Worth-Arlington	2.86
25	Austin-Round Rock	2.43

Source: U.S. Census Bureau and Real Estate Center at Texas A&M University

The net rental yields in Table 5 are before-tax net rental yields because the net rental incomes are before taxes.

When considering a home as an investment, keep in mind that real estate properties are the least liquid investments and rental incomes and owner costs are volatile. Compare price appreciation to general inflation, tax considerations and capital gains.

Given that an owner-occupied home provides shelter for a long time, gains from housing as an investment are valuable additional advantages for homeowners.

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