

It Still Makes Sense to Buy versus Rent

Nearly a full third of households are still renting...but if you are one of them, you could be paying a hefty price. Additionally, the children of the baby boomer generation are close to or at the home buying age, but these "echo boomers" could mistakenly decide to put off the purchase of a home because of all the noise about a "bubble" in home prices.

Is there a "bubble"? The simple answer is "no". Even if interest rates move a bit higher, it won't be enough to cause a nationwide slide in home prices. The key to a healthy housing market is the job market. If the payment on a new home might be slightly higher due to increased interest rates, it generally won't stop someone from purchasing the home of their dreams...but if they feel their job is in jeopardy, it might be enough to stop them from making a move. So with the currently low levels of unemployment and the beefy gains in job creations, it looks like the housing market will remain vibrant. Although it will be difficult to sustain the double-digit gains that much of the country has seen, price declines are highly unlikely. Expect a more moderate rate of appreciation, perhaps closer to the historical 6-7% range, which is still very good.

It is important to note that housing tends to be localized. So if the job market in your area is weak, housing prices could under perform the rest of the country.

But this talk of a housing bubble has been going on for a few years now, and those who were unfortunately victimized by continuing to rent instead of purchasing a home are painfully mulling over their missed opportunity. But is it too late? Even with the more moderate levels of appreciation expected...procrastinating on that home purchase could cost you a bundle.

Let's look at an example. If you are paying rent at \$1,500 per month and your landlord increases your payment by a modest 5% each year, you would wind up paying just about \$100,000 over a 5-year period! Worse yet, after forking over \$100,000, you still would have nothing to show for it.

And speaking of having nothing to show for it - how about any improvements you might make to a rental property? It's not uncommon for renters to freshen up the paint, install new light fixtures or plant some nice flowers outside. But guess what...all your efforts, labor and the benefit of that improvement belong to the landlord, not to you.

With the extensive variety of programs to help buyers obtain a mortgage with little to even zero down payment, the very same money could have been used towards home ownership. Even using a standard 30-year fixed program, a mortgage of \$300,000 could be obtained with a total monthly mortgage payment - including property taxes and insurance - of around \$2,200. Assuming a 25% tax bracket, this would be equivalent to the average amount spent on rent during the same period after your tax benefit.

And the benefits of home ownership are quite considerable. Because the mortgage is being paid down each month, equity is being built. After 5-years, the \$300,000 mortgage

would be reduced to \$279,000, adding \$21,000 to your net worth. Home appreciation can add an even bigger chunk. If your home appreciates at a modest 5% per year, the value of a \$300,000 home would increase to \$383,000 after 5-years. Subtract the remaining mortgage of \$279,000 and you have a whopping \$104,000 of additional net worth! Even if the appreciation level were at 3.5% or half the historical norm, the result would be \$77,000 of additional net worth.

But if laying out the initial increase in monthly payment and having to wait for your tax benefit to show up next April is a tough nut to crack, the IRS wants to help. Instead of waiting to file for the tax benefits derived from your new home purchase, you can simply adjust the amount of your withholding. This allows you to have less tax withheld from each paycheck so you can handle the new mortgage payment more comfortably throughout the year. In essence, you are taking your tax refund as you go instead of letting Uncle Sam hold it all year, interest free.

Visit www.irs.gov and use the IRS withholding calculator. This very handy tool can quickly show you the effect a change in withholding will do to your net paycheck. Remember to balance this with the expected refund and it is always a good idea to check with your tax advisor.

Don't be victimized by the bubble hype. Buying a home is a big step, but it is almost always one in the right direction.