THINGS TO CONSIDER IF YOU ARE BUYING A HOME

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THE PRICE IS THE SAME, BUT THE COST IS LESS

There is more and more research coming out showing that it makes great financial sense to purchase a home today. Whether it is Rent vs. Buy ratios, income-to-price ratios or income-to-mortgage payment ratios, purchasing a home right now is a bargain compared to historic norms. Now, you should to look at the COST of a home today compared to pre-peak prices.

According to the S&P Case Shiller price index, residential real estate values have returned to 2003 first quarter prices. That, in itself, says something. However, when you factor in mortgage rates, the case for buying a home today becomes even more compelling.

In 2003, 30 year mortgage rates stood at 5.88%. Today, they are 4%. How does that impact the actual COST of a home? On a home purchased for $250,000, here is the difference in monthly cost:

DATE	LOAN AMOUNT	INTEREST RATE	MONTHLY PAYMENT (P&I)
2003	$250,000	5.88 %	$1,478.84
Today	$250,000	4.00 %	$1,193.54
Difference in Mortgage Payments			$285.30

That means you save $285.30 a month, $3,423.60 a year and $102,708 over the life of a 30 year mortgage! **You buy the home for the same PRICE but the COST is over $100,000 less.**

This is why so many financial advisors are saying that this may be **one of the greatest times in history to purchase a home.**

WILL THE 30 YEAR MORTGAGE DISAPPEAR?

The federal government is reconsidering their involvement in the home mortgage process. They plan to still 'guarantee' certain mortgages. However, they appear to be redefining what they consider a 'qualified purchaser'. They are discussing stricter lending guidelines in four different areas:

1. **The type of mortgage**
2. **The minimum down payment**
3. **The debt ratios of the buyer**
4. **The FICO score of the purchaser**

It appears that there is at least conversation about eliminating the 30 year fixed rate mortgage which has been a staple in this country's housing industry for some time. Some in government want to duplicate the mortgage process of other countries. In Canada, for example, they don't even have 30 year fix rate mortgages available. The vast majority of Canadian home loans have a 25 year payout but the interest rate is renegotiated every five years. If rates go down, you will wind up with a lower rate. If rates go up, you end up paying a higher rate. If you want a fixed rate mortgage for 25 years you pay a rate approximately two percentage points higher than the going rate at the time of your closing.

Would the same happen in this country? Housing Wire quoted Janis Bowdler, senior policy analyst at the *National Council of La Raza*:

> *"Without some form of Fannie Mae and Freddie Mac, replacements to support these popular loans, many first time borrowers will be shut out."*

> *"Without that guarantee lenders would not offer 30-year fixed-rate mortgages, at least not at rates the average person could afford. Yes, some would be available but not for the average family but for those with a large amount of inherited wealth they can put to a large down payment."*

WHY IS THIS IMPORTANT?

You probably want to set your housing expense at the lowest number possible for the longest time possible. This may be the appropriate time to lock-in your long term housing expense as three things seem possible, if not likely, in the future:

- **Mortgage rates will increase from current historic lows**
- **The 30 year fixed rate mortgage may disappear**
- **Rents will return to historic norms of 3% annual increases**

If you want to purchase a home of your own but are waiting to see where prices will go, consider what you could be giving up while you wait.

TIPS TO PRESENT A STRONGER MORTGAGE APPLICATION

As underwriting guidelines for lenders become more stringent, we need to re-examine what a good mortgage application looks like. As home buyers begin their search for a home, there are a few items they should be aware of that they can do to help get their loans approved (with the best possible terms), and, at the same time, lessen some of the stress that goes along with the mortgage process.

1. INCOME DOCUMENTS

Most lenders want to see a full month of paystubs and two years' complete Federal Tax Returns. Assembling them ahead of time and holding on to every paystub you get is a good idea even before you find a home and/or submit your mortgage application because it will save you time later. Moreover, looking at those documents and being prepared to explain any deductions that show up is crucial. Child support, alimony, garnishments, and unreimbursed employee expenses are often crippling factors that, if explained and dealt with upfront, can make your loan approval smoother.

2. ASSET DOCUMENTS

Most lenders will scour your bank accounts for the two months prior to going to contract. They are looking for large deposits because large deposits can signal a new loan that wouldn't show up on your credit report yet. What's a "large deposit"? Typically, any deposit that would represent more than your income can support. If you make $5000 a month, after taxes you likely net $3800 (or $1900 a bi-weekly pay period). Therefore, deposits in excess of that will need to be explained and documented. Sold a motorcycle? Have a paid receipt and motor vehicle documents in place. Received a gift? You will need a Gift Affidavit, proof of the donor's ability and transfer of the funds. Any and all questions should be discussed with your loan officer.

3. CREDIT SCORE OPTIMIZATION

Do your best to curtail your use of credit as it relates to your available credit lines. Target a cap of 30% of usage of available lines to get the best scores. Do NOT cancel credit cards. That will lower your amount of available credit, thereby raising your percentage of usage. That will damage your score. Do NOT shop for a car, explore life insurance, apply for a new credit card or increase the limits on your current cards because the running of your credit by people in other industries will also lower your credit score. Most importantly, don't do anything that will require having your credit run without first discussing it with a mortgage professional who knows the impact it could have.

4. APPRAISAL CONCERNS

It's unlikely you will make an offer to purchase without checking out comparable home sales. It's also likely you received that type of data from the real estate agent you are working with. Make sure your agent prepares the same information for the appraiser. Data about similar sales, similar homes currently on the market and maybe even cost estimates for any repairs or improvements anticipated can preempt future problems with appraised values and conditions. Overall, it is recommended that you hold onto copies of everything financial. Think before allowing your credit to be run and work with an agent and loan officer who can use their experience to put your loan application in its best possible light... as soon as you start thinking about buying a home.

REAL ESATE:
GOLDEN OPPORTUNITY
OF THIS DECADE

Everyone wants to comment on the current real estate market. They want to talk about how now is not the time to buy a home. Some even argue owning a house has never been a great investment. Most say it will be a long time before real estate again begins to appreciate. It all sounds so familiar to me. It was just a decade ago that many made the same arguments about gold as an investment.

Gold had dropped from over $400 an ounce to $250 an ounce (a 40% decline) from February 1996 to August 1999. People ran from gold as though it was a plague.

Lord William Rees-Mogg, the current Chairman of *The Zurich Club*, in 1997 said:

> *"No investment has been so thoroughly exploded as gold; most people think that there will no more be another gold boom than there will be another boom in tulip futures in The Netherlands."*

Two years later in 1999, Don Wolanchuk author of the *Wolanchuk* Report explained:

> *"Everybody hates gold. You can't have a bottom until everybody is out. And everybody is out of the gold sector."*

Everyone knows what happened next. The proclamation of gold's death was rather premature. Gold rose from $250 an ounce to over $1,400 an ounce in the next twelve years. I see the same situation with real estate today. I am not predicting that real estate will see the same levels of appreciation. I do believe however that the market will rebound strongly.

Those who continued to believe in gold as an investment were rewarded. Those who continue to believe in real estate as a sound investment will also be rewarded.

Here is what Adam Hamilton wrote in October 2000 in an essay titled **Is Gold Dead?** :

> *The road for gold investors has been long and parched in the last five years. They have wandered through a seemingly endless desert, occasionally tempted by what proves to be an illusory mirage. Many have fallen beside the sun-cracked path, their white bones picked clean by buzzards and gleaming in the sun. Nevertheless, a brave contrarian core continues to march forward. They have studied history, currency, gold, investments, economics, and finance. They understand the timeless value of gold, the cyclical nature of the markets, and the vagaries of human psychology. They realize it is darkest before the dawn, and the journey most difficult right before the homestretch is reached.*
>
> *Gold is in an INCREDIBLE position, and it will have its day. Nothing goes up in price forever, and nothing goes down in price forever. Investments are cyclical. Gold is NOT dead, it is simply biding its time, waiting for its next earth-shattering mega-rally. The spoils that go to the few remaining gold investors when that day inevitably arrives will be fantastic. The stunning victory will quickly blot out the painful memories of the long struggle…*

You could replace the word 'gold' with the words 'real estate' throughout this essay and it would apply today.

IS IT REALLY TIME TO BUY A HOME?

A recent report by *JP Morgan* explains the reasons why now is a great time to buy a home. Right from the beginning, the paper identifies the greatest challenge in today's housing market: consumer emotion. They attempt to overcome that emotion with logical explanations. They break it down to the following.

PRICE-TO-INCOME RATIO

One measure of housing values is the ratio of personal income to home prices. The report explains where we are today:

> *"Since 1966, the median price of an existing single family home in the U.S. has varied between 150% and 251% of personal income per household. However, roughly three-quarters of the time it has been in a relatively narrow band between 185% and 230%."*

Today the ratio is just 153%, implying that to get back to an average price to income ratio, home prices would have to rise by about 27%.

CURRENT MORTGAGE INTEREST RATES

With current 30 year mortgage rates, housing payments are at historic lows as compared to personal income. With interest rates at about 4%, they explained:

> *"Assuming the use of a fixed rate mortgage with 20% down, this would make the median mortgage payment on a single family existing home just 6.9% of per household personal income, compared with an average of 14.4% since 1966."*

MONTHLY RENT VS. MONTHLY MORTGAGE PAYMENT

Is it less expensive to own a home or rent a home? The answer to this question helps families make the decision whether or not to buy a home. The report explains:

> *"…we estimate that the implied median mortgage payment has fallen to just 78% of the median asking rent…"*

The paper comes to the conclusion that now is the time to buy.

> *"The numbers on housing have an important message for American families today, and particularly younger families setting out on life's great adventure: Five years ago, at the peak of the home-buying euphoria, it was emphatically a time to rent. Today, when home ownership is depreciated more than ever before, the numbers tell us it is a time to buy."*

AMERICANS STILL BELIEVE IN THE VALUE OF HOMEOWNERSHIP

Fannie Mae 's **National Housing Survey** questions the American public on a multitude of questions concerning today's housing market. We like to pull out some of the findings we deem most interesting.

Here are some of the most interesting findings from their most recent report:

MOST IMPORTANT REASONS TO BUY A HOME

The study shows that the four major reasons a person buys a home have nothing to do with money. The top four reasons, in order, are:

- **It means having a good place to raise children and provide them with a good education**
- **You have a physical structure where you and your family feel safe**
- **It allows you to have more space for your family**
- **It gives you control of what you do with your living space (renovations and updates)**

When we talk about homeownership today, it seems that the financial aspects always jump to the front of the discussion. There is no doubt that families must justify a home purchase from a financial point of view today. However, the reasons they actually buy are the same reasons our parents and grandparents purchased their home – to create a better lifestyle for their families.

THE HOME AS AN INVESTMENT

Though most people purchase a home for non-financial reasons, everyone realizes there is a money component to homeownership. Here is what they said on this issue:

- **64% of the general population (and 69% of homeowners) believe that homeownership is a 'safe' investment.**
- **55% believe that homeownership has more potential as an investment than any other traditional asset class.**
- **68% think that now is a good time to buy a home**

RENT VS. BUY

- **63% of renters have aspirations to someday own their own home**
- **70% of renters think that owning is superior to renting**
- **96% of homeowners see homeownership as a positive experience (4% see it as a negative experience) while 83% of renters see renting as a positive experience (15% see it as a negative experience)**
- **97% of homeowners live in a single family residence while 53% of renters live in a multi-unit building**

Even in these difficult times, Americans still realize the value of homeownership both from a financial and social standpoint.