

THE ARIZONA REPUBLIC

Is This a Good Time to Buy a House? (Part 2)

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In the previous article (8/19/09) I discussed whether it is time to buy a home. The three issues to consider were: do you believe that home prices have stopped dropping; what type of home will you buy (REO-lender owned, short sale, or normal property); and do you feel secure about your future job or income. This article will consider some other critical issues:

1. Do you have enough money to cover the down payment, closing costs, moving, and slight fix-up costs? The lowest down payment available (3.5%) is with a FHA loan. Closing costs can add 3%, and slight fix-up costs (such as painting, new carpets & tile, and small repairs) can add another 2.5%. On a \$250,000 purchase price, this could total 9% cash required, or \$22,500.

In some cases, one can negotiate for motivated sellers to pay the 3% closing costs. One can also pay a higher price for a home fully fixed up and ready to move in. In this optimal situation, the 3.5% down payment would still be \$8,750. One also should have a cash reserve of at least the next 2-3 mortgage payments. This would be about another \$3,000-4,500. Given the serious recession of the last 2 years, many buyers would need to have \$11,750-13,250 cash available.

If you qualify as a first-time homebuyer (meaning you have not owned a primary residence within the last 2 years), you could qualify to distribute \$10,000 from your IRA. Even if you are under age 59.5, you would be exempt from the 10% penalty. If both

you and your spouse are first-time homebuyers, each of you can receive distributions of up to \$10,000 for a first home without having to pay the 10% penalty. However, you will have taxable income to the extent that you withdraw the \$10,000/spouse who qualifies.

2. Can you qualify for a mortgage loan? After the Mortgage Meltdown during the last 3 years, when over 200 lenders have gone out of business, underwriting criteria are back to the old days. One now must document everything on the loan application with wage statements, tax returns, and proof of sufficient assets (bank accounts, IRA and 401(k) statements, stock brokerage accounts...). One must also have a good credit history and have a low total debt-to-income ratio.

3. Do you believe that mortgage rates will increase substantially in the next 1-5 years? Right now, a borrower with very good credit could get a FHA mortgage for about a 6.0% rate (including the monthly mandatory mortgage insurance premium). On a \$241,500 30-year amortized mortgage (\$250,000 purchase price), the monthly payments would be \$1,446.42.

If future rates went to 7.5%, the monthly payment would increase to \$1,686.60, an extra \$240.44/month. To maintain one's monthly payment at \$1,446.42 in a 7.5% interest rate world, the loan amount would reduce to \$206,863.56. With a standard FHA loan requiring 3.5% down, this would translate to a \$214,366 purchase price,



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instead of the former \$250,000. One would get a substantially different house at the cheaper price.

4. Are you ready to live a long time (typically at least 5-7 years) in the home? Virtually everyone hates moving. Real estate is not liquid. The costs to sell a home can reach 10% of the sales price, when one adds the 6% real estate commission, fix-up, and closing costs. If real estate prices do not appreciate more than 10% before you sell, you will lose money.

Conclusion: Buying a home is a very serious decision, now that qualifying for a mortgage can be difficult and we're in a serious recession. The decision will often rely on family conditions, such as wanting a stable situation to raise kids in a good school district.

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