

Money

February 18, 2021

The Math Is Changing on Whether It's Better to Buy or Rent a Home



As people flock to the suburbs due to the pandemic, home prices have shot up and rents slacked across the United States.

And yet, owning a median-priced, three-bedroom home is still more affordable than renting in roughly two-thirds of the country, according to a new analysis of 2020 numbers by real estate data company ATTOM Data Solutions. A year ago, owning was more affordable in just over half of the counties ATTOM analyzed. This is despite the fact that median home prices rose faster than both average rent and average wages in most places.

That's because mortgage rates have plummeted over the last year. In July 2020, the average rate offered to well qualified borrowers fell below 3% for the first time ever and hit an all-time low of 2.65% in January 2021. Though rising, rates are still low, providing home shoppers with cheap money.

"Your monthly mortgage payment has been moving down, just because mortgage rates are so low," said Todd Teta, chief product officer at ATTOM. "That's what's offsetting home price increases and making ownership still very affordable in a lot of the United States."

Driven by low rates and the ability to work from home due to COVID-19, many urbanites left city rentals to buy homes in the suburbs. ATTOM found that affordable homes for purchase are still concentrated in suburban areas. People who moved from the city to the suburbs were often able to buy larger homes for better prices per square foot.

Even those who chose to rent in the burbs are often paying less, despite the fact that rents in secondary and suburban markets are growing faster than in the cities, according to a new report by listing site realtor.com.

Rent posted large declines in major cities such as Los Angeles, Seattle and New York, but renting in those places remains more attainable than buying. Sale prices drastically dropped in the biggest cities early in the pandemic, but have started to rebound and are still generally higher than in the suburbs.

To determine which option is more affordable in a given place, ATTOM compares what percentage of the local monthly average wage is needed to cover rent versus the share needed for the typical mortgage payment.

For example, in Manhattan, the average rent eats up about 28% of average wages in the borough, while owning the median price home requires a whopping 96%, according to ATTOM. In contrast, an hour west in Sussex County, New Jersey, the dynamic reverses. The average rent is about 52% of monthly wages there. But monthly home-owning expenses are 44%.

Of course, deciding whether renting or buying is right for you involves more than just a price comparison. Here are some other questions to consider.

Are you going to live in a home for at least 5 years?

Regardless of how low your monthly mortgage payment is, it typically takes several years for a house purchase to actually pay off. That's due to the high upfront costs of buying a home, as well as the regular expenses of homeownership.

Closing expenses at time of purchase can total 5% of the sale price. Then, there are property taxes and home insurance premiums, which vary by locale. The expense many new homeowners are not prepared to handle, however, is maintenance, which averaged about \$3,000 in 2020, according to home improvement marketplace HomeAdvisor.

"If you expect to be mobile and move within a window of roughly five years or less, you're probably better off renting only because the costs associated with homeownership are significant," said George Ratiu, senior economist with realtor.com.

To calculate how long a homeowner need to hold onto a property for owning to become more affordable than renting, realtor.com compares the costs of buying (a down payment, mortgage outlays, maintenance costs as well as property taxes and insurance) to the expenses of leasing (such as a security deposit, renter's insurance and monthly rent).

Taking inflation, interest rates and equity building into account, the firm's buy-vs-rent calculator can help house hunters determine their own breakeven point.

In expensive metros, it can take much longer than five years to justify a home purchase. For instance, in Manhattan, owning becomes cheaper than renting after 12 years on average, according to realtor.com. In contrast, in Raleigh, North Carolina, it only takes four years for buying to pay off.

Do you have your financial house in order?

According to a recent survey by loan marketplace LendEDU, 55% of new homeowners now regret taking out a mortgage during the current economic downturn. Most of them cited pandemic-induced financial woes as the source of their remorse.

Ratiu advises renters to tidy up their financial house before buying a house. Would-be homeowners should pay down existing debt, stash away emergency savings and money for as large a down payment as possible.

While some lenders allow for down payments as low as 3% and sometimes less, "the larger the down payment, the better," said Ratiu. Conventional home loans typically require 20% down to avoid paying mortgage insurance. Plus, the more home buyers pay upfront, the smaller their monthly payments.

Experts say that, whether owning or renting, people ideally would not spend more than a third of their income on home-related expenses. Anything above that threshold would constitute a housing-cost burden.

When it comes to emergency cash reserves, personal finance experts recommend having enough to cover living expenses for three to six months. As a homeowner, you'll want at least that in order to cover maintenance and unexpected repairs.

What are your life goals and investment strategy?

Saving for a sizable down payment takes time and effort. Sometimes, these funds can be put to a better use depending on personal goals. Leasing an apartment can provide renters the opportunity to "use their money in other

ways, whether it's investing in the market or starting a business," said **Stephanie Kanner**, broker with **Fox Residential** in New York City.

In fact, over the long run, stock investing is often more profitable than buying a residence, especially after accounting for homeownership costs. Although home prices have risen quite a bit since the Great Recession, historically, home-value appreciation tends to be lower than what the stock market returns.

However, the question of whether to buy a home — and when exactly do it — often transcends investment strategy. "The majority of people are not solely making a financial decision," said Teta. "They are generally making a life decision and then making a decision on renting versus buying."

The decision to buy is often tied to milestones that require more space, such as getting married or starting a family. Yet, it also bears monetary repercussions based on local market dynamics.

If your company allows you to work from home after the pandemic, should you buy a house?

Because of the pandemic, droves of urban renters decided to relocate to the suburbs and small towns. Lifestyle changes such as working from home, which some companies are now adopting as a routine policy, are incentivizing home purchases in towns that are more affordable than major cities.

But Douglas Elliman real estate agent Stacey Oestreich says that home shoppers moving to new areas should consider renting for a while, even if they have the means to buy a house. This strategy allows would-be homeowners to "test-drive" a neighborhood, its schools and amenities.

"Renting gives you the flexibility to make the right decision," she said. "The single biggest decision anyone has to make is, 'Where do I want my family to live?' If you don't know, renting takes a little bit of the pressure off."

<https://money.com/cheaper-to-buy-or-rent/>