A House for Your Family: Buy or Rent?[1]

Virginia Peart and Marie S. Hammer[2]

The questions of what kind of house, how large a house, or even whether or not to own a house are based on more than just economic factors.

There are advantages and disadvantages in both owning and renting, but most people put a high value on home ownership. The desire to own one's home has long been a part of "the American dream."

What Are the Advantages of Home Ownership?

- Home ownership represents a form of forced savings; many families would never accumulate assets otherwise.
- Mortgage payments contribute to an investment, particularly if the property is located where it increases in value over a period of years.
- Interest and taxes are legitimate income tax deductions.
- Equity in a home improves the credit status of the family and could be used as collateral for an emergency loan.
- Housing costs, with a fixed rate mortgage, are stabilized because present and future costs can be estimated and planned.
- Home ownership contributes to security, especially in retirement years when income normally decreases.
- Home ownership generally strengthens social and financial standing in the community.
- Home ownership contributes to general well-being and "roots" of the family, especially for children.
- There is freedom to change the house and surroundings as desired.
- Homeowners are generally more concerned about community affairs.

These and more reasons for home ownership can be cited, but many other factors must also be considered.

Deciding to buy or rent will involve, perhaps, the largest amounts of money the family will spend and involves a long-term commitment of both time and money.

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2. Written by Virginia Peart, former associate professor, Housing and revised by Marie S. Hammer, professor, Housing/Home Environment, Department of Family, Youth and Community Sciences, Cooperative Extension Service, Institute of Food and Agricultural Sciences, University of Florida, Gainesville, 32611.

How Much House Can a Family Afford?

American consumers spend from 21 to 54 percent of family income on housing. How much each family spends on housing depends on many factors. Three basic considerations that can help a family determine how much house they can afford are:

- The amount of take-home pay that the family can reasonably expect.
- The family's living costs and other debt payments.
- The **total** amount of housing expenses, including taxes, insurance, energy, furnishings, maintenance, mortgage payments, and management fees if you live in a condominium or planned development.

Because of rising prices and increased housing-related expenses, the old rules-of-thumb on how much to pay for a house no longer apply. Lenders usually follow two basic guidelines in determining how large a mortgage to grant:

- Principal, interest, taxes and insurance (PITI) should not exceed 25 to 29 percent of gross income; and
- PITI **plus** other long-term debt should not exceed 33 to 41 percent of gross income.

Long-term debt includes car and installment loans, alimony, child support, and charge card balances that will take more than 10 months to repay.

The range the lender uses will depend on the size of the down payment. Lenders probably will use the 28-percent and the 36-percent figures if you are paying 10 percent down. If you are paying 5 percent down, lenders will probably use the more conservative 25 percent and 33 percent. FHA loans use 29 percent and 41 percent.

These are general guidelines used by lending institutions. The prospective buyer should use these guidelines and then evaluate them in terms of the family: size, stage of life cycle, job stability, amount of savings, present spending pattern, and lifestyle.

To estimate how much house you can afford, first follow the example at the end of this publication for a family with a gross annual income of $20,000 annually for a 30-year loan at 9 percent interest. Then, enter your gross annual income in the Blank A space and follow the instructions.

Are You Ready for Home Ownership?

In deciding whether you are in a good position to buy a house, ask yourself the following questions:

- Are you sure you want to buy a house?
- Do you have steady income and stable employment?
- Do you anticipate remaining in the same geographic location for the next couple of years?
- Have you created a budget so you know how much you can realistically afford to pay for housing?
- Do you have an established credit record or can you build a non-traditional credit history with records of payments to previous landlords and utility companies? If so, is your credit profile favorable? Do you pay on time or before the due date?
- Do you have enough money saved up for a down payment and closing costs? If not, can you enlist the aid of relatives or government or non-profit agencies that might give or loan you money?
- Have you been "pre-qualified" by a lender so you know how much you can borrow based on your income and existing debt?
- Is your existing debt low enough that it will not limit your ability to qualify for a mortgage? If not, can you pay down your debt before you attempt to buy a house?

• Have you looked into the benefits and requirements of the numerous financing options that are now available to low- and moderate-income home buyers?

If you can answer "yes" to all of these questions, you may be well on your way to owning your own home!

If you cannot answer "yes" to these questions, be an informed renter.

For Renters

Make yourself familiar with the following terms relating to rental of housing:

Contract Rent — Rent contracted for by the renter which may or may not include heating fuel, cooking fuel, electricity, water, furniture or other services.

Lease — Contract between owners and renters of properties stipulating rents to be paid, condition of the property, and other responsibilities of each party. There is NO such thing as a standard lease. Read your lease carefully! Feel free to work out a mutually satisfying lease.

Lessee — Person meeting the terms of the lease — the renter and tenant.

Lessor — Person granting the lease — the landlord or owner.

Rent — Fixed periodic payment received by the owner of the property from the user, for its use.

Renewal of Lease — Terms should be outlined in the lease which will specify if the renewal is yearly or monthly. Renewal may be automatic unless the management is given written notification within 30 to 60 days before the expiration date. Again, read the lease!

Security Deposit — One or two months' rent as a guarantee that the tenant will stay during the full period of the lease and that the apartment will be maintained as rented.

Sublease — An agreement transferring all or part of the rights of a tenant of a house, apartment, or other building to another party.

Terminating a Lease — If the landlord chooses not to accept renewal, he can notify the tenant to vacate. Check the lease for this clause.

Townhouse — Contemporary version of the row house, usually rented but sometimes sold. The rows commonly include from four to ten units, two or three stories high, with some front lawn and an enclosed rear yard area. Common walls between units cut down on noise and upkeep. The greatest saving is in land cost. Exterior design varies from ultramodern to the "Colonial look."

Considerations for Buyers and Renters

Neighborhood

- Location
- Appearance
- Residents with similar occupational and social interests
- If buying, whether area is appreciating or depreciating in value
- Safety and security

Accessibility

- Convenience to work, shopping areas, school, and church
- Good roads and streets

Community Facilities

- Police and fire stations
- Health and sanitation services
- Schools, churches, and other desired facilities
- Parks and recreation areas

Family Values

- Appearance
- Size versus amenities
- Special features your family needs

Costs

- Amount within the figure determined as your maximum
- Cost of money — both interest rate and terms
- Tax benefits
- Energy costs

Dwelling Itself

- Space, arrangement, and condition
- Bedrooms — enough space and privacy
- Kitchen and work area — well-planned and step-saving, with adequate work and storage areas
- Dining and living areas — adequate for family entertaining
- Storage — adequate and well placed in each area of the house
- Room sizes, shapes, and wall areas to permit use of furnishings and equipment on hand or planned
- Interior and exterior finishes — types acceptable, condition good, easy maintenance
- Heating and lighting — adequate and efficient systems

How Much House Can I Afford?

It is smart to estimate what you can afford to pay before you begin to look at houses. Here is how to use the 28 percent guideline used by mortgage lenders. By putting in your annual income, you can estimate what your monthly payments should be. Follow the example in Table 1. Then complete the form in Table 2. Table 3 is the Rate Factor Chart.

Table 1.

Example: A. Gross Annual Income.	$20,000
B. Gross Monthly Income. $20,000 divided by 12.	$ 1,667
C. Monthly Allowable Housing Expense. $1,667 multiplied by .28 which should include PITI.	$ 467
D. Monthly Principal and Interest Payment. $467 multiplied by .90. 90% includes PI and excludes TI.	$ 420
E. Estimated Mortgage Amount. $420 divided by 8.05 (Factor from chart for a 9% loan amortized over a 30-year term) multiplied by 1,000.	$52,174
F. Affordable Price Range. $52,174 divided by .90. 90% is the customer mortgage loan amount, assuming 10% down payment.	$57,971

Table 2.

Your Estimate A. Gross Annual Income	$
B. Gross Monthly Income. A. divided by 12	$
C. Monthly Allowable Housing Expense. B. multiplied by .28	$
D. Monthly Principal and Interest Payment. C. multiplied by .90	$
E. Estimated Mortgage Amount. D. divided by Factor from chart multiplied by 1000 (See Chart for Factor Amount)	$
F. Affordable Price Range. E. divided by .90	$

Table 3.

RATE FACTOR CHART

Interest Rate	15yr	25yr	30yr
6 percent	8.44	6.44	6.00
7 percent	9.00	7.07	6.65
8 percent	9.56	7.72	7.34
9 percent	10.14	8.39	8.05
10 percent	10.75	9.09	8.78