Ownership just isn't the same

Alter your budget for that new home

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Rearranging budget priorities is sometimes necessary when a family changes from tenant to home owner status. The status switch often involves acquiring such major appliances as washers and dryers or other items that renters don't normally own.

However, this initial period of a slightly different budget passes and, barring historically higher mortgage interest rates such as those experienced in the latter part of 1981 and the first half of 1982, a family can settle down to a fairly regular and predictable schedule of cash outlays.

For one thing the price of the home is fixed and is a permanent hedge against inflation. Unlike rent, which is forever on the upswing, the price cannot be changed once the new owner takes over. Of course, should the purchaser decide to sell at any time in the future, he is entitled to the profit resulting from the increased value of his property.

There have been many discussions comparing the merits of owning to the merits of renting. The investment aspect and control over price are two reasons why the majority of dwelling units in this country are owner-occupied, attesting to the value Canadians place on home ownership.

Traditionally, the average price of homes has escalated with almost every passing year. Between 1971 and 1981 the average price of properties processed through the MULTIPLE LISTING SERVICE by real estate boards which are members of The Canadian Real Estate Association more than tripled. Average prices increased from $24,581 to $78,486, making buying property a good investment.

ONLY A MEMORY

There was a time more than 30 years ago before mortgage interest rates reached the 10 per cent mark (a level that would be considered low today), that the term of the mortgage loan and the amortization period coincided. A borrower paid the same interest and made the same monthly payment for as long as it took to pay off the mortgage, whether it was 20, 25 or even 30 years. The mortgage never had to be renewed.

Economic conditions don't remain static, however, and mortgage lenders of the 1980s don't and won't gamble that interest rates will remain static for an indefinite period into the future. So instead of having mortgages at a fixed rate of interest for a couple of decades of tomorrows, five years is now the longest period a lender will accept and not all of them will gamble on conditions that far ahead.

The net result is there are usually at least four different mortgage interest rates at each lending institution: one for a year, another for a two year loan, still another for three years, and again one for five years. The longer the period of the loan, the higher the rate, thus protecting the lender if rates suddenly take off. The terms of the loans don't mean they are paid off in that period of time, only that they have to be renewed at rates then current when the term expires. The actual repayment period could be over any number of years, but usually 20 or 25.

All of this is a familiar — but not necessarily a welcome — experience for home owners who have to renew their mortgages and must decide which term at which rate they are going to take. When mortgage rates zoomed into the stratosphere last year many home owners found themselves having to readjust their budgets to make higher payments if their mortgages came due for renewal.

In some cases a wife will rejoin the labor force with the single-minded purpose of paying off the mortgage, so that it will cease being an expense at the earliest possible moment.

Bearing in mind that mortgage payments are made with after tax dollars, the last example where savings represent $110,113.80 equals after tax earnings of more than $22,000 a year for five years. The savings could provide an excellent basis for a retirement or investment program working for the home owner instead of for the mortgage company.

To demonstrate how ridiculously small the difference in monthly payments can be in relation to the period of amortization, one only has to look at the contrast between 25 and 50 years. At a 15 per cent interest rate the monthly payment on a $60,000 mortgage is $747.79 over a 25-year repayment period, as previously mentioned. On a repayment period of 50 years the monthly payment is reduced to $728.11. But the interest paid over the full term increases from $164,307 to $376,866 — a difference of $212,559 to reduce monthly payments by less than $20.00!

Is any more convincing argument needed to pay off a mortgage as quickly as possible?

CROSSWORD CORNER

Crossword Puzzle Answer on Page D10