
WE WOULD LIKE TO
EXTEND A BIG THANK
YOU TO THOSE OF YOU
THAT HAVE REFERRED
FRIENDS & FAMILY

CALLING ALL MOVE-UP BUYERS

NOW MIGHT BE THE RIGHT TIME TO BUY

(Even if You Think Housing Prices
Have Further To Fall!)

By Chris Butaud, Guild Mortgage

I cannot tell you how many times I have heard the best Realtors I know offer some variation of this advice to their would-be clients—“Don’t sell now unless you have to.” While this may be commendable advice for its obvious emphasis of the client’s interests over the Realtor’s, that alone does not make it good.

For all of its simplistic appeal, waiting until we reach the bottom of

the market before selling your current home and purchasing your move-up home may not necessarily yield the best overall result. The reason for this is that even relatively modest increases in financing costs can far outweigh the benefit of a lower purchase price.

Consider the example of a buyer who wishes to purchase a \$650,000 home with a \$450,000 home to sell, and finances that new purchase with a down payment from the proceeds of the current home. Even under extremely pessimistic assumptions of additional housing price declines of 7.5% over each of the next two years, this purchaser is money ahead (in less than

CURRENT INTEREST RATES:

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CHRIS BUTAUD

NMLS #13157

GUILD MORTGAGE

(206) 999-6941

CBUTAUD@GUILDMORTGAGE.NET

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CALLING ALL MOVE-UP BUYERS (CONTINUED)

10 years) by buying now if interest rates rise just $\frac{3}{4}$ of 1% per year during that same two-year period.

BREAKING DOWN THE GRAPH

The purpose of the graph (opposite) is to provide an apples-to-apples comparison of the total economic impact over a 10-year period of buying a house now vs. waiting one or two years to buy that same house. The elements of the chart are:

- Blue line representing the equity in a move-up home that is purchased now (Year 0)
- Red line representing the equity in the same move-up home that is purchased one year later (Year 1)
- Green line representing the equity in the same move-up home that is purchased two years later (Year 2) and presumably at the bottom of the market.
- Adjusted Book Equity (vertical axis) is the net proceeds from the sale of your current home that are re-invested in the move-up home
- Years in New Home (horizontal axis) is self-explanatory
- The chart assumes that the real estate market will continue to decline a total of 15% over the next two years, and then remain essentially flat for the period.

The easiest thing to do (and just about the only thing many people do) is to compare the purchase price now vs. what the price will be if the market continues to fall. If the market suffers an additional 15% decline

over two years, the buyer who waits two years will have saved himself almost \$100K on a \$650K house. Who wants to waste \$100K? Case closed, right?

Not so fast! Unless the house you are selling is located on another planet, you will also lose 15% of its equity in the same two-year period and suddenly the \$100K is closer to 30. Still nothing to sneeze at, right? Sure. But here's the rub: What if interest rates rise over that same period of time?

IMPACT OF INCREASED FINANCING COSTS

This is where the "buy now vs. later" analysis understandably breaks down for many buyers. After all, what is a 1.5% increase in interest rates compared to a \$30K discount on the purchase price?

Great question! For starters, a 1.5% increase over today's prevailing rates represents about a 38% increase in financing costs. What's more, unlike housing price changes which are a one-time factor, increased financing costs continue to impact your housing equity for as long as you have the loan—potentially as long as 30 years. Consider a simple example of a 1% increase in interest rates on a \$400K loan amount. Over a 10-year period, a buyer will pay almost \$40K in additional interest, and more every year until the loan is paid off.

BACK TO THE CHARTED EXAMPLE

In the example given at the opening of this article, the move-up buyer sells his or her home for \$450,000 and purchases a move-up home of \$650,000 now rather than waiting (blue line).

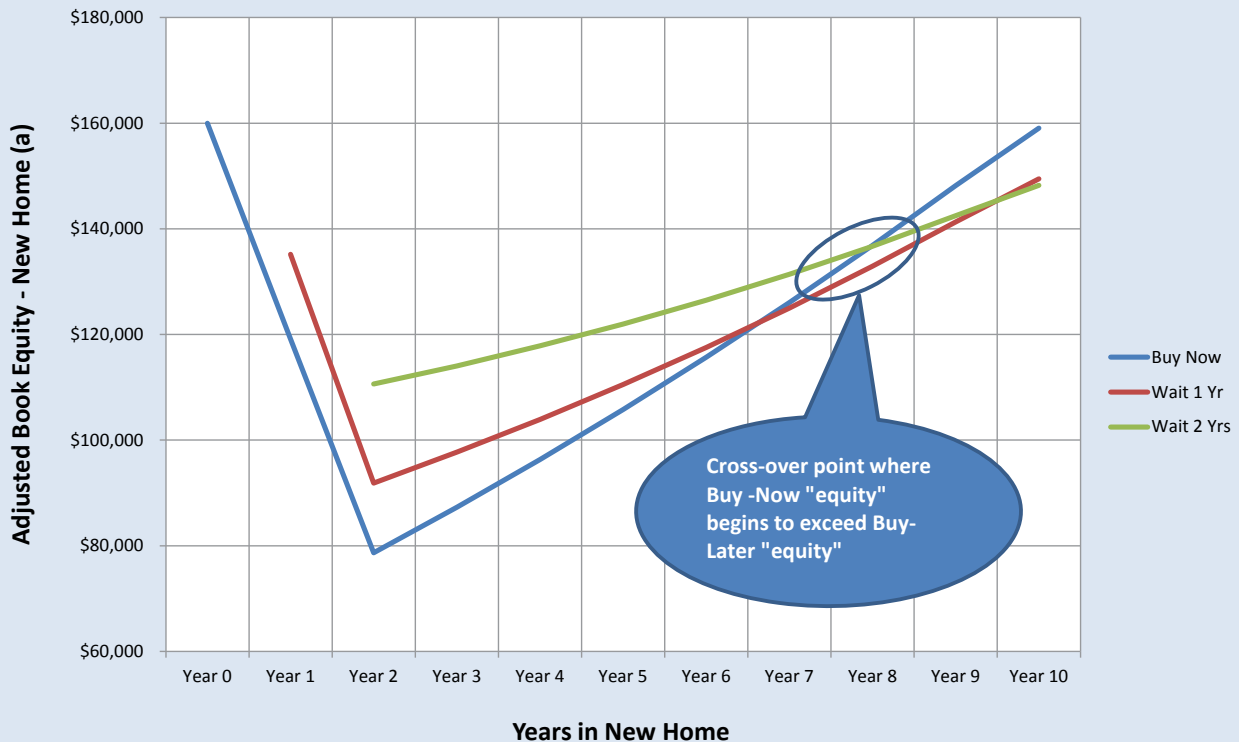
We will assume a net equity of \$160,000 out of the existing home to be applied to the move-up home. Note

Move-Up Analysis

10 Year Comparison

based on

15% Real Estate Market Decline Over the Next 2 Years



that because of the continued market decline, the equity diminishes to approximately \$80,000 by the end of year two in the new home. But by year eight, that equity has returned to a value that begins to exceed the equity value in the same home which was purchased either one or two years later—by the buyer hoping to take advantage of the reduced price in one year or the bottom of the market in two years. Since every home is unique, and you happen to find a move-up home in the very near future that just captivates you, it just might make financial sense to purchase now rather than wait.

ABOUT THE AUTHOR

In this newsletter, we have invited Chris Butaud with Guild Mortgage to contribute an article that encapsulates his recent research on the question of whether to consider a move-up home purchase decision now, or to wait for the market to continue its decline before purchasing either a year later, or even two years later.

We have been honored to be able to refer our clients to Chris Butaud over the past 12 years. Chris came into the mortgage industry after 27 year career as a CPA, and his performance for our clients has been of the highest caliber that we could possibly hope for. Chris also brings a dedication to the industry and integrity to life in general that we find few that will match.

Chris holds a master's degree in taxation from Golden State University, and a bachelor's degree in accounting from Washington State University.

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