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It's a great time to buy your first home

Prices, mortgage rates and tax credits look ideal for first-time homebuyers

Brian J. O'Connor / Detroit News Finance Editor

Would-be first-time homebuyers who've been sitting on the sidelines waiting for just the right moment to jump into the real estate market should get ready to pounce.

The backlog of homes for sale in southeastern Michigan is down, while prices and mortgage interest rates are creeping up. Meanwhile, the federal first-time homebuyers credit can give you \$8,000 to help with the down payment, closing costs or fix-up bills for your new home sweet home.

"You can find unbelievable deals out there in great neighborhoods," says Harry J. Glanz, co-founder of Capital Mortgage Funding in Southfield. "If you have a job and a down payment, you're going to get a nice property for a much, much lower price than you would have three or four years ago. And you're going to get an \$8,000 tax credit right away."

In May, the number of homes for sale in the region dropped to the lowest level in four years, according to the RealComp multiple listing service. The median sales price increased, with prices on non-foreclosed homes rising to \$110,000, the highest level this year. Meanwhile, homes are selling faster, too, at an average of slightly more than three months.

Despite the uptick, sale prices still are lower than a year ago. But mortgage rates have risen, up 30 basis points last week for a 30-year loan, to 5.95 percent nationally, according to Bankrate.com, and 5.875 percent for Metro Detroit.

While it's impossible to predict if home prices and sales have bottomed out, it all indicates that this is a good time to buy and may be the best time to come for a while. Even with slightly higher rates, a home loan of less than 6 percent still is one of the lowest rates in the last 40 years.

Good credit and a job also are needed

But as much as the home market has changed, so has the world of mortgage lending. Zero-down

loans are pretty much a thing of the past. Expect to put a minimum of 3.5 percent down under FHA programs, as well as closing costs that averaged about \$2,200 in Michigan last year, according to Bankrate.com, excluding and points paid on the mortgage.

Unlike the days of the subprime mortgage boom, buyers also will need good credit and a job or some other way to prove they can repay the loan, Glanz advises.

"There's no such thing as 'got no job, we don't care,' " he says. "At some places, all you needed was a pulse. The mortgage landscape is not that way anymore, but good people with good credit can still get loans."

Good credit means a credit score of 650 or better, Glanz says, and certainly not less than 580, which is into subprime territory. You can buy a copy of your credit score or have a mortgage agent check it as part of getting pre-approved for a loan. If your score comes back too low, focus your efforts on boosting your credit before calling a real estate agent.

New tax credit eases purchase

While credit is tighter, coming up with down payment cash is easier, thanks to the new tax credit. A first-time homebuyer -- anyone who hasn't owned a home for at least the past three years -- can get a refundable \$8,000 tax credit on next year's return. If you don't want to wait, amend your 2008 return to get your money before January by filing IRS Form 1040-X.

You have to purchase the home first to get the credit, but the FHA has just rolled out guidelines to allow lenders to advance the tax credit to homebuyers. That catch is that while that money can be used to pay closing costs and mortgage points, it can't be counted toward the FHA's 3.5 percent down payment minimum, and borrowers can't get any cash back.

Putting the money toward upping the down payment will help lower your monthly mortgage payments, but it might be wiser to use your tax refund to bolster your emergency savings account, and set aside money to deal with the inevitable repairs and emergencies that inevitably come with home ownership, warns Dale Vermillion, author of "Navigating the Mortgage Maze: The Simple Truth About Financing Your Home" and the web site, Mortgagempowered.com.

"One of the most common mistakes people make when they buy a home is they take all their cash reserves and then have nothing to fall back on," Vermillion says. "That's very dangerous."

Other financial dangers in buying a first home are purchasing more house than you can afford, getting hit with unexpected closing costs, property taxes or insurance premiums, and failing to budget for repairs and maintenance, he says.

Calculate your ceiling

To avoid the missteps that have swelled the foreclosure rates, buyers should budget first, shop later. First calculate what kind of interest rate you'll pay and how that translates into your monthly payment, with principal, interest, taxes and insurance. Then shop for a home where the monthly payment equals no more than 20 percent to 25 percent of your gross monthly income, even though Realtors and mortgage lenders will say you're qualified to borrow more.

"People buy more home than they can afford," Vermillion says. "Set a budget before you even begin looking."

Also budget for home fix-up costs, which average 1 percent to 2 percent of the purchase price each year. "If you're planning on less than \$200 a month you're making a mistake," he says.

If possible, ask the owner for a list of repairs and improvements made in the past two years. Then get a detailed estimate of repairs the home will need, based on a visit from an experience, certified home inspector, and budget for that, too.

Finally, ditch the notion that your home will be an investment, even if it's a rock-bottom foreclosure. Buy in a stable neighborhood where you want to live, getting a home you can take care of where you'll be comfortable and can afford to stay for at least the next five years.

The main message for first-time buyers is that even though bargains are to be had, they need to do their homework. The mortgage mania of the past few years is over, but buying a home can still be complicated and costly. Work with experienced, reputable real estate agents, mortgage lenders, appraisers and inspectors, experts say, and you can navigate the process with no surprises and few disappointments.

"Combine the tax credit with mortgage rates that are still low and prices that are really down from where they were," Vermillion says, "and those things make for a really good buying market."

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