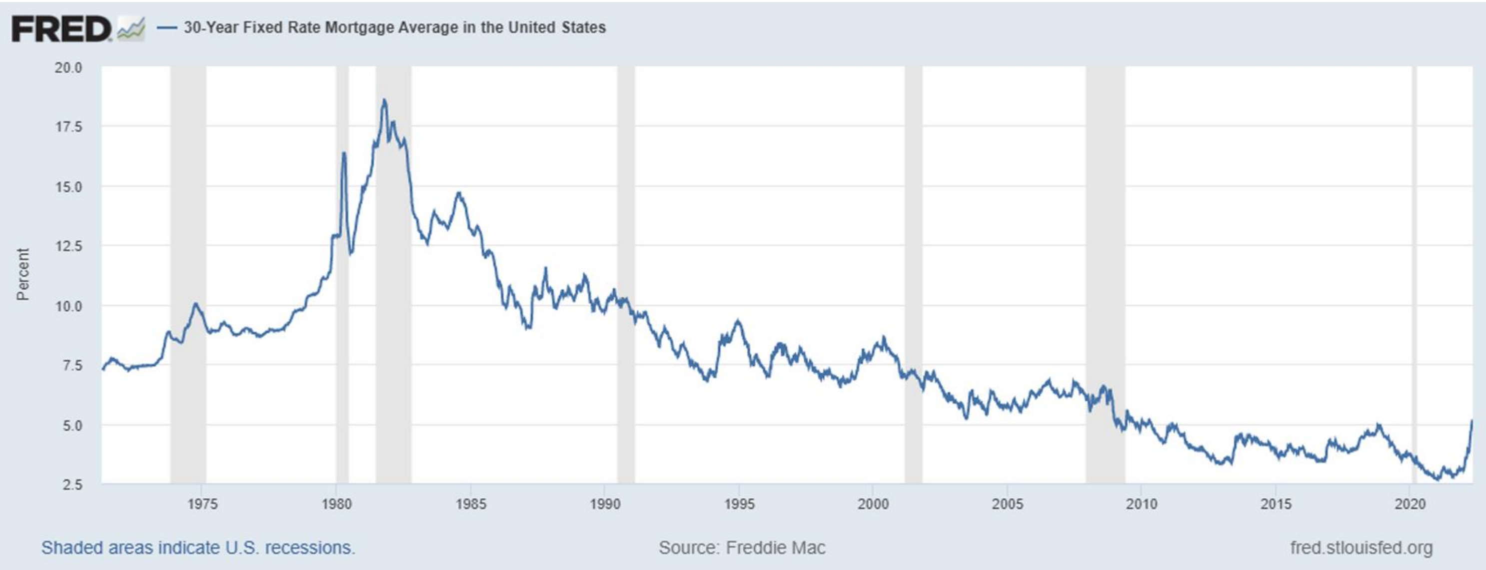
Interest Rates Going Up…

In most simplistic terms, when the fed raises interest to slow down inflation, the interest rate goes up on mortgages. This makes it more costly for consumers to purchase a home. When homes are more expensive, the demand for them decreases. This results in a slump in the housing market…On the opposing side, if demand is so high, ***supply is low, and the cost to build a new home is going up due to cost of land, building material, labor***…this causes the price of existing and new homes to climb!

So, interest rates were in the 2.6% range in December of 2021, now 5 months later we are in the 5-6% range. (For the most popular 30-year conventional loan), and how does this affect the buyer?



Most buyers are more concerned about the monthly payment than the actual interest rate. Remember, the mortgage is one part of the payment to live in a home. There are also utilities, insurance, taxes, sometimes PMI (if the down payment is less than 20%) not to mention food, clothing, car payments etc.…1% increase in rates, translates to approximately to ***11% higher monthly payment***

What most shoppers don't realize is how dramatically their buying power is diminished with relatively small rate increases.

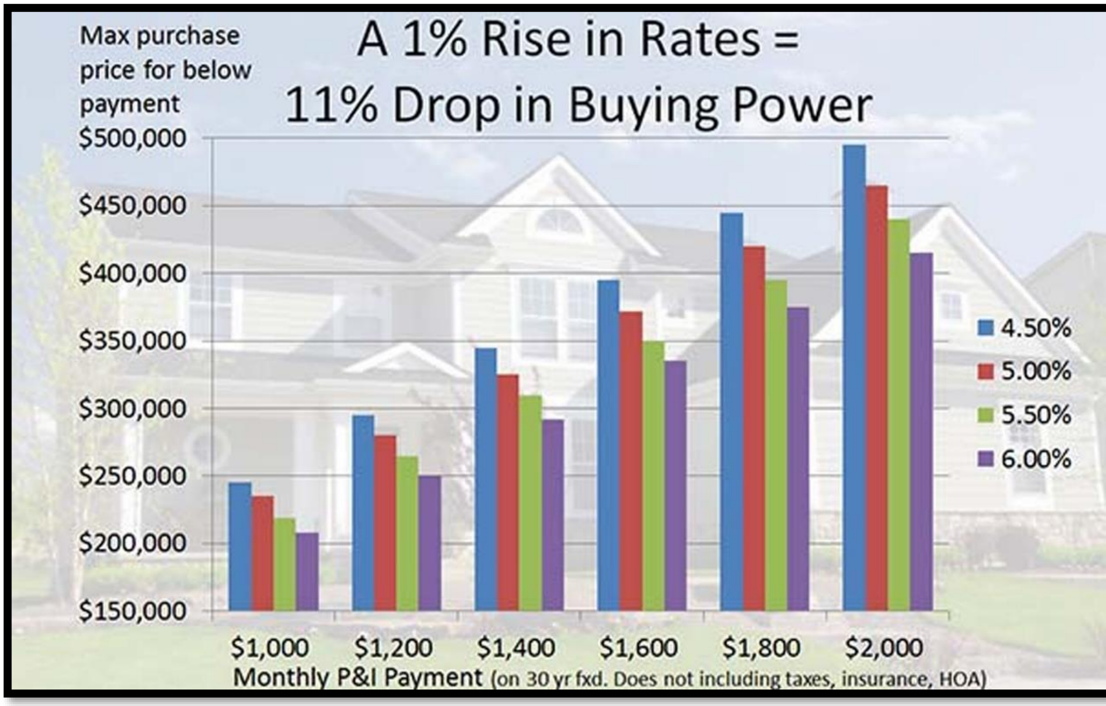
Let's imagine you had $1,200 per month to spend on your principal and interest payment. (Keep in mind this number doesn't include things like property tax, insurance, mortgage insurance, or HOA dues).

That $1,200 per month can go a long way when rates are low. For instance, if you locked in a 30-year fixed mortgage at 4.5%, you could buy a house for $295,000 if you had 20% down. But let's say rates rise to 5.5%. Still a great rate, but 1% higher than you planned.

Now you are limited to a purchase price of $265,000, again assuming 20% down. ***That's a 10.17% reduction in buying power*** and $30,000 shaved off your maximum purchase price. At $1,800 per month and 20% down, you could buy a home for $445,000 with a 4.5% interest rate. But at 5.5% your maximum home price is now $395,000 – ***an 11.24% reduction in buying power.***

At the lower end of the spectrum, $1,000 per month would buy you a $235,000 home at 5.0% but just a $208,000 home at 6.0%. That's an 11.49% reduction and in some areas could make the difference between getting into a home or not, or settling for less house.

A rate increase could harm your buying power more than increasing home prices. ***It's unlikely home prices would rise by more than 10% in a year, but if rates increase by 1% it will have the same effect for buyers.***



As you move to higher purchase prices, the sheer dollar amount that is shaved off your purchase price by rising rates is pretty incredible.

You could buy a $420,000 home at 5.0% if your budget were $1,800 per month. But at 6.0%, your purchase price is $375,000, a reduction of $45,000. At a $2,000 per month payment, your maximum purchase price is cut by over $50,000 by a 1% increase in rates. These are big numbers and could affect your ability to get into the home you wanted, or into a home at all in higher-priced areas.

Give us a call, if you are thinking of selling or buying…interest rates may not be coming down for a while!

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