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This may be golden age for first-time home buyers

By Ron Lieber
New York Times News Service

Five or 10 years from now, when the financial crisis has ended and housing prices are up smartly once more, we will look in the rearview mirror and realize that we missed a golden age for first-time homebuyers.

Then, everyone who sat on their down-payment savings accounts for a few years too long will kick themselves for not taking advantage of what may turn out to be the buying opportunity of a lifetime for those who can qualify for a mortgage.

Unfortunately, we do not know when this golden age will begin, because we will be able to identify a bottom to the housing market only with the benefit of hindsight.

But as it does with the stock market, the moment will probably arrive when everyone is feeling the most pessimistic.

That moment is certainly getting closer. Housing prices have fallen drastically from their peak levels in many areas of the country. Rates on conventional 30-year fixed-rate mortgages are already close to 5.5 percent, and there has been talk recently that the federal government might try to drive them down to 4.5 percent, a truly incredible figure to be able to lock in for three decades.

Meanwhile, first-time homebuyers have the same advantage they have always had, which is that they do not have to sell their old place before buying a new one. That is an added advantage in areas where many available houses simply are not moving, because the people trying to sell them will not be bidding against you.

If you're hoping for a recovery in the housing market, you ought to be cheering on the first-time homebuyers. When they purchase homes, their sellers are free to move on or move up, stimulating further sales.

But if you are a potential first-time buyer yourself, or lending or giving the down payment to one, you are probably as frightened as you are tempted by all the "For Sale" signs that have become "On Sale" signs.

So let's quickly review some of the still-grim pricing data in certain areas — and consider the reasoning offered up by first-time buyers who have forged ahead anyhow.

Think practical

As is always the case with real estate, much depends on location.

One study, "The Changing Prospects for Building Home Equity," tries to predict where today's first-time buyers in the 100 biggest metropolitan areas may actually have less home equity by 2012 as a result of continued price declines.

The verdict: Buyers in 33 of the markets could see a decline by 2012, including potential six-figure drops on an average home in the New York City, Los Angeles, San Francisco and Seattle metropolitan areas.

This is obviously scary. It's worth noting, however, that these predictions came before the government made its most recent move to push down borrowing costs.

Also, the price projections in the study are based, in part, on the fact that the ratio of purchase prices to annual rents is still much higher in many areas than the historical average, when homes sold for roughly 15 times rents.

While past figures may well have some predictive value, I have never been convinced that first-time buyers compare a home that they could own and one that they would rent in purely or even primarily economic terms.

When Jaime and Michael Proman moved this fall to Minneapolis, his hometown, from New York City, they craved a different sort of life after two years together in a 450-square-foot studio apartment that had no room for their wedding gifts. "We didn't want a sterile apartment feel," said Michael Proman, who is 28 (his wife is 26). "We wanted something that was permanent and very much a reflection of us."

The fact is, in many parts of the country there are few if any attractive rentals for people looking to put down roots and enjoy the sort of amenities they may spot on cable television home-improvement shows.

Comparing a rental with a place that you may own seems almost pointless in these situations, especially for those who want to make their own decisions about décor without consulting the landlord.

Still, for anyone feeling the urge to buy, a number of practical considerations have changed in the last year or two. The basics are back, like the idea of spending no more than 28 percent of your pretax income on mortgage payments, taxes and insurance.

Even if a lender does not hold you to this when you go in for pre-approval on a loan, you should hold yourself to it.

You will also want to start now on any credit-score improvement project, because it may take several months to get it above the 720 level that qualifies you for many of the best mortgage rates.

John Ulzheimer, president of consumer education for credit.com, a consumer-credit information and application site, suggests paying down and putting away credit cards starting months before you apply for a home loan.

That is because the FICO credit-scoring system could penalize you if you use a lot of your available credit each month, even if you always pay the bill in full.

Also, check your three credit reports (it's free) at www.annualcreditreport.com and dispute any errors that may be hurting your score.

Mitigating risk

While no one can easily predict the likelihood of losing a job, the rising unemployment rate suggests the need for caution if you think you might be vulnerable. A.C. Panella, who teaches communications at Pasadena City College in California, waited until she had a tenure-track job before buying a home in Los Angeles with her partner, Amy Goldman, who is a lawyer for a nonprofit organization.

"We could afford the mortgage payment on one salary were something to come up," said Panella, who is 31. "It's really about being able to stay within our means."

For many first-time homebuyers, that philosophy now stretches to the down payment, too. Panella and her partner put down 20 percent when they bought their home in September, as did the Promans when they bought their home in Minneapolis.

Alison Nowak, 29, put just 3 percent down on a Federal Housing Administration-backed loan last month, when she and her partner, Lacey Mamak, bought a \$149,900, 800-square-foot home. "Anything that is an opportunity also has a bit of risk," she said of her house, which had been in foreclosure before a plumber bought it and fixed it up. "One way we mitigated it was that we bought a really tiny house in a very good neighborhood."

One other risk-mitigation strategy in the coming months might be to buy new instead of used. Ian Shepherdson, chief U.S. economist for the research firm High Frequency Economics, says he believes that a steep drop-off in inventory of new homes is coming soon, thanks to a rapid decrease in homebuilder activity.

Since prices generally soften in the winter, it may make sense to start looking seriously once the mercury bottoms out.

"If you look at new developments next spring, you may not have the choice you thought you would have or be in the bargaining position you thought you would be," Shepherdson said.

Also, if you wait after June 30, you will miss out on a \$7,500 federal tax credit for income-eligible first-time homebuyers that works like an interest-free loan.

Finally, allow yourself to consider how it would feel if you bought and then prices dropped another 10 or 15 percent. It might not bother you at all if you plan to stick around for a while.

Plenty of people seem to be making a longer commitment to their homes than they used to. According to a survey that the National Association of Realtors released last month, typical first-time buyers plan to stay in their home 10 years, up from seven just last year.

Perhaps people are more aware that they will not be able to build equity as rapidly as others did during the real-estate boom years. Or they simply have more confidence in hard, hometown assets right now than they do in other markets.

"We wouldn't let another decline bother us," said Proman. "You can never time a bottom. This is a long-term investment for us, and it truly is the best investment we have in our portfolio right now."

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