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PURCHASE OF HOUSE AND FINANCING OF IT AND OWNING AND LIVING IN IT FOR, SAY, 55 YEARS
RECENTLY, WITH A GROUP OF PEOPLE, THE SUBJECT OF HOME OWNERSHIP CAME UP AND THERE WAS A LOT OF INTEREST ON IN THE OUTCOME WHICH I HAVE RECORDED AS FOLLOWS.

Key starting points:

(1) 30 year old couple who have saved up $125,000 to purchase a house on the fringe of a New Zealand city, costing $625,000.

(2) The couple have two children aged 3 years and 5 years - he is working 40 hours per week and she is working 30 hours per week - their combined income is presently $101,400 per year (before tax).

(3) They are finding child support is expensive and are not saving anything at present, but this will change and when it does she will increase her hours.

(4) They have borrowed $500,000 from their bank presently at 3.85% but are not making any loan principal repayments at present, but their bank has talked about 2% a year which is $10,000.

(5) The house insurance and rates on the house at present are $6,800 per year. The house is only ten years old such that the repairs and maintenance as yet have not surfaced.

(6) They are not far away from both sets of parents and the schools are close by and there is a university approximately 28 kilometres away.

(7) They each have a car, but no expensive hobbies.

(8) Both enjoy their present jobs where each have been employed for some ten years - they feel they may inherit maybe $75,000 each from their respective parents but not for maybe 25 - 30 years as both parents are 60 years old.

(9) They are okay with money but will never be high earners, but should live completely within their income - they talk about having their present mortgage repaid by the time they are both 70 years of age - but that is 40 years away and would involve an average annual bank mortgage repayment of $12,500 per year which, at present, looks a little unlikely but possible.

(10) They each have pure term life assurance of $250,000 which would halve the bank term loan if the worst happened and have health insurance covering 85% of all surgery costs for themselves and their two children - the present annual cost for all this is $3,300 per year.

(11) The question that was raised at the meeting is what will be the total cost of the house if they live in it until they are both 85 years old - that is 55 years from now.

(12) These people at the meeting were involved in housing, insurance and banking so there was quite a cross section of advice and experience present - it was agreed, though, that I would put something down on paper for the group at our next meeting to criticize.

Given these comments, facts and assumptions, this is my assessment:

(a)	House deposit	$125,000
(b)	House bank term loan ($500,000)	-
(c)	Term loan repayment - 40 years at $12,500 per year	$500,000
(d)	Interest payments (say, based on $250,000 because of the annual principal repayments having been made of $12,500 per year - 55 years x 3.85% x $250,000)	$529,375
(e)	Rates and insurance (55 years at $6,800)	$374,000
(f)	Repairs and maintenance - hard to say, but say (55 years x $1,500 per year)	$82,500
(g)	Allowance for unforeseen (say, 55 years at $500 per year)	$27,500
(h)	House renovations (say 3 times over the 55 years at $15,000 each time)	$45,000
		$1,683,375
	Less residual value of house and section, say, in 55 years' time (65 years old - section would be worth more but house maybe less (say) (see point (4) below)	$625,000
	Total cost over 55 years ($18,643 per year) - ($359 per week)	$1,025,375
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Notes:

(1) Everything is in today's dollars - these costs will all probably rise, but probably at a similar rate to their rise in wages.

(2) What might it have cost to rent for 55 years regarding a similar house (say 55 years x $500 per week x 52) - $1,430,000.

(3) Renting would look some $400,000 more expensive, although they could downsize for perhaps their final 25 years.

(4) The 'rule of 72' suggests that if the inflation rate is 1.5% over the 55 year period that the house and section, if well maintained, could have a residual value in today's dollars of $1,350,000 ($625,000 x 'rule of 72'). I have though not allowed for any inflation adjustment of any kind and simply taken the view that the house and section in 55 year's time will be worth as much as it cost – that is $625,000. To be fair though, there are many 65 year old houses (built in 1964 in this case) that are still selling at well above their original costs – consequently, my residual value figure of $625,000 may well be conservative, which would mean the margin in favour of owning would be higher than $400,000.

(5) Looking forward for 55 years is impossible – perhaps though one could say that it is hard to see how renting could ever be cheaper than ownership long term.

Some very broad assumptions here, but owning for you, your children and grandchildren would still look the best option from a cold blooded financial point of view.

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