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Homeowners: Will Selling then Buying Back Later Save You Money?

The concept of selling to your property to rent, whilst prices fall, then buying at the bottom of the market may seem a licence to print money. Initially you must agree with the doom mongers not the optimists. Indeed market analysts seem split between slight price rises in 2005 – 2006 and serious price falls.

CML: +4%, Haart estate agents: +3-5%, RICS: +3%, Nationwide: +2%,. FPD Savills: +2%, CEBR: Up +1.3%, Halifax: -2%, Capital Economics: -7%, Barclays: Down -10%.

Some predict longer term losses over the next 2-3 years or longer term gains. Unsurprisingly mortgage brokers and Estate Agents seem more optimistic whilst economists and stock brokers take a dimmer view.

Indeed recent reports suggest property prices in central London are only 12% higher now than at the end of 1999. This would suggest London has already experienced a soft landing. West End offices are being let at record levels with demand up 63% on 2003 in 2004. This should indicate employment growth and corporate confidence. Graduate salaries with some City Banks now offer £32,000 p.a. with a £3,000 golden hello, rising to £45,000 in three years. One bedroom flats in Highbury N5, a traditional first time buy for City workers with a future eye on well healed central Islington, are selling for around £210,000. After a few years renting the price to income ratio looks relatively attractive at 4.6.

However for the sake of this report let's assume prices crash 10% over a one or two year cycle. What real savings can be made, if any? Unfortunately you will not save a simple 10% by selling, renting, waiting, then buying due to the related costs of selling property, buying property, and rent. Property is certainly not the most liquid asset, like stocks and shares. We also presume the seller is an owner occupier who needs another property to rent. Furthermore the intention must be to buy a similar property at a lower price. If you are selling a buy to let (consider rental voids and capital gains tax), can move in with a friend, are selling to trade up, or have a second home to occupy the figures adjust dramatically.

Savings / Gains

- The difference between the sales price before the crash and the buy back price after, 10% of the property value.
- Interest on the cash sum of your sale less the mortgage, assuming the cash is sensibly placed in a high interest savings account at 5% (ING Barings)
- Mortgage Payments assuming a repayment loan at 5% interest.

Rising interest rates have been good for savers so any cash generated will earn a few thousand per annum, less tax of course. An ISA will protect savings from Tax however only a limited amount may be housed in such a vehicle, typically £3,000 per annum.

Expenses relating to sale and purchase:

- Estate Agency fees typically 2% of the property value plus VAT (17.5%).
- Legal fees for selling property typically £1000.
- Mortgage redemption fees often around £150. However this could be more depending on your current product. Indeed many discount or fixed rate products have especially painful early redemption penalties.
- Rent depends on the property however we assume a like for like exchange, so for a £200,000 flat we assume a weekly rent of £225 and so on. You could save more by temporarily renting a bed-sit however this might not be everyone's idea of fun, nor

entirely practical for those with a family. You could however severely compromise your location.

- Lettings Agency administration typically £200.
- Legal cost for buying new property another £1000.
- Mortgage Broker Fees £250, if any.
- Mortgage Arrangement Fee £350, if any.
- Homebuyers Report £500, we assume any buyer will desire a good level of survey
- Stamp duty for new property 1% up to £250,000 3% up to £500,000, 4% above.
- Tax on savings interest from savings, charged at 20%
- You could try to sell your property privately hence avoiding Estate Agency Fees. Indeed you could attempt to complete your own conveyance to save further fees. Both short cuts are possible but very time consuming and could simply result in excessive wasted time.

We examined four different property values £200,000, 350,000, £475,000, and £600,000. For each price we examined different mortgage levels: no mortgage, 50% mortgage, and an 80% mortgage. Each scenario was considered over one and two years.

Results:	**1 year**		**2 years**		
Property value:					
£200,000 no mortgage	£6,350 saved	3.2%	-£5,350	cost	-2.7%
£200,000 50% mortgage	£9,445 saved	4.7%	£4,840	saved	2.4%
£200,000 80% mortgage	£12,721 saved	6.4%	£13,793	saved	6.9%
£350,000 no mortgage	£8,375 saved	2.4%	-£11,125	cost	-3.2%
£350,000 50% mortgage	£13792 saved	3.9%	£6,708	saved	1.9%
£350,000 80% mortgage	£17,074 saved	4.9%	£17,408	saved	5.0%
£475,000 no mortgage	£12,023 saved	2.5%	-£15,018	cost	-3.2%
£475,000 50% mortgage	£19,374 saved	4.1%	£9,185	saved	1.9%
£475,000 80% mortgage	£23,784 saved	5.0%	£23,706	saved	5.0%
£600,000 no mortgage	£8,450 saved	1.4%	£-27,950	cost	-4.7%
£600,000 50% mortgage	£17,736 saved	3.0%	£2,621	saved	0.04%
£600,000 80% mortgage	£23,307 saved	3.9%	£20,964	saved	3.5%

On face value the results are impressive the cash sums indicate a significant saving. However as a percentage the figures seem less exciting. Indeed the major correlation seems to occur between outstanding mortgage amounts, the more you owe on your mortgage the more you save as mortgages costs are currently comparable to rent. However should you own your property outright and hence pay no mortgage, rent significantly erodes any saving. The interest on your invested cash sum increases, but not at the same rate as rent. Typically an interest rate of 7.5% is required for interest to equal rent on a mortgage free property, 15% interest for a 50% mortgaged property, and well over 20% interest for 80% mortgaged properties.

Indeed if the compare percentage savings with level of outstanding mortgage:

1 Year		**2 Years**	
No mortgage	2.38%	No mortgage	-3.42%
50% Mortgage	2.94%	50% Mortgage	1.2%
80% Mortgage	5.03%	80% Mortgage	5.09%

Variables

- Interest rate fluctuations could save or cost money over time.

- The upward trend of rental prices may erode savings further.

- Tenants do not pay service charges or ground rent so a significant saving can be made. However in essence rent usually absorbs the service charge.

- Owners with interest only mortgages will pay significantly less in mortgage payments hence, in the short term, losing more in terms of mortgage payment versus rent.

- Additional associated costs of moving may be incurred: two removal vans (£99 per day), extra solicitor's fees for complicated sales (£750), any rental deposit lost due to excessive wear and tear.

- If you have a repayment mortgage you are constantly paying off the loan, therefore after one or two years the amount outstanding will have decreased.

- Property in your area may fall more than 10% or significantly less.

- Political changes: should Labour fail to win a third term the preceding government may reduce stamp duty, or eliminate it entirely for first time buyer.

- In a poor or falling market Estate Agents, Mortgage Brokers, Solicitors, Conveyance firms, lenders, and alike may reduce their fees to attract business.

- Credit rating: credit rating agencies and mortgage lenders generally penalise applicants who frequently change address. If your credit rating isn't fantastic you could dent it further by moving twice in a relatively short time span. If you do move be sure to register on the voters roll, for council tax, and clear all utility bills. Such loose ends could restrict you credit worthiness and product choice (the best mortgage deals are often saved for the most credit worthy) when buying.

- Indeed the sluggishness of the sales process may mitigate any saving. For example you sell now yet it takes six months to complete the sale. As the market drops your buyer negotiates a slight discount just before exchange, you have no option but to agree. Who else will buy in such a slow and falling market? Once the market has bottomed out you try to buy however can't find the right property. Once found the market may be firming and the buyer may demand full asking price. Immediately prior to exchange the vendor demands a slight increase as the market is rising. Any saving is immediately lost and an extended rental period presumably increase those losses.

- If you plan to rent for more than a year there is no guarantee the landlord will renew your lease. They may need the property back after a year or in a strong rental market demand a higher rent to renew. You may move three times in all adding to the stress of the exercise, and incurring additional costs.

- Notice: tenants must give landlords a clear moths notice before vacating, to coincide with the commencement date of the lease. Furthermore a landlord may demand a fixed year or six month tenancy. With exchange and completion dates so variable in the property sales process, you could be left owing the landlord several months rent after your planned completion. Or having given notice to the landlord, have the deal fall through. It could be time to sweet talk the landlord and let you stay, or start looking for a new rental property.

- Tangible Emotional Loss: most owner occupiers like their property, indeed they bought it in the first place. There is no guarantee that you'll find the right property at the bottom of the market. This downturn is not due to a collapsing economy, many do not need to sell, and therefore fewer properties may enter the market. Losing your perfect home, and the stress of moving at least twice, may prove so stressful any finical gain seems insignificant.

- Opportunity Cost: would you gain financially using the time spent selling/renting/waiting/buying to peruse other avenues? Indeed the process will take considerable time. If you invest the time at work, or in your business, will you gain more? Maybe work hard and gain promotion? Put time into your business and increase profits? Will you seen distracted at work, could your future earnings suffer? Will your business suffer if you're off viewing property during the day?

- Preference: If your selling to become a long term "good time renter", someone who wants to rent to increase their life enjoyment. Renting offers fantastic flexibility: no maintenance costs, no stamp duty, service charges, or mortgage deposits. You could sell now, live all over London for 2-3 years experiencing all it has to offer, then buy again without missing significant capital growth. It could be a fun few years, six months in Soho, six months in Kensington, then six months in Hackney. It might help you buy the perfect property when you re enter the market.

Are There Any Situations Where the Concept Really Succeeds?

If you do sell, rent, wait, buy you may want to buy a more expensive property after your rental period. Waiting to trade up will certainly save money long term. Having no chain and a large deposit will make you very attractive to vendors. Furthermore the higher price the larger the discount as a percentage after predicted price falls.

Indeed sell a £200,000 property with a 50% mortgage, wait a year while renting as prices fall. Then buy a £400,000 property (Now priced at £360,000) and save £25,845 after associated move costs. Alternatively loose £11,700 in terms of rent if the market holds steady or even loose £11,700 plus the additional cost of the new property if prices actually rise.

Debt consolidation: if the owner is paying large interest payments on credit cards, personal loans, or other debts. Paying these off with the proceeds of a property sale will no doubt save money long term. The freedom of heavy interest payments should quickly transform the seller's presumably limited disposable income, and enable saving. Provided the market drops the seller should be able to buy back in a stronger position with a similar mortgage. Property transaction costs are at least one off. However those without a significant mortgage may be better advised to withdrawer equity to consolidate such debts provided the credit lines are not simply reused.

Conclusions

Owners with no mortgage will not make significant savings by selling, renting, buying. Indeed rather than sell they might be better to re mortgage and invest in something more interesting with a good potential for growth. This will of course depend entirely on their attitude to risk.

50% mortgages could make some savings although the 2% - 3% pocketed seems slight. More could be saved by simply finding a better mortgage deal, saving more disposable income to pay off the mortgage quicker, or investing in Tax Free investment vehicles.

80% mortgages certainly save the most and the lower the property value the better, higher stamp duty levels severely erode savings at the upper end of the property ladder. However the overall 5%+ is hardly overwhelming.

The London market would need to drop 15% to achieve truly significant savings of 8%-10%. Although in such a market rental values should escalate alarmingly.

To achieve any saving timing must be perfect, selling at the right time then buying at the right time, with no hitches during the sales process.

The idea should appeal most to buyers looking to trade up.

Finally

The market has to fall by 10% in the first place. Selling, renting, waiting, buying is an awfully time consuming and stressful process, especially if you depart and re-enter the market at the same or a higher level.