

I've bought a house: my worst ever financial decision



Merryn Somerset Webb
Investing

We've just bought a house. It is exactly the kind of house we have long wanted to live in, so we are thrilled. But I am also pretty sure that, while buying it might be a good thing for family stability, it will also be the worst financial decision we have ever made.

You don't need to know that the average house price is still well over five times the average income – or that the average first-time buyer was forced to put down a deposit of £50,000 in March, or even that more than 80 per cent

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of adults under 30 are unable to afford to buy any kind of house in the UK, according to the National Housing Federation – to know that house prices are still in bubble territory. Instead, you just need to look in an estate agent's window. That usually does it.

That said, markets keep showing us that things can stay at the "wrong" price for years. So, saying that house prices are too high isn't necessarily the same as saying they are going to fall. For that, we need a trigger of some kind – such as the subprime crisis that kicked off collapse in the US and a mini shock in our own market.

It is always tricky to spot the trigger in advance, but there does seem to be an unusually dangerous number of contenders at the moment.

Might it be the funding gap? Mortgage approvals for house purchases are still exceptionally low, yet mortgage lenders are even now warning that they could get lower thanks to a £400bn funding gap currently being filled by the Bank of England support schemes

introduced at the peak of the financial crisis. These schemes will soon end and the new government has made no mention of extending them. Perhaps it will. But if it doesn't, the past few years of mortgage drought might in retrospect look like something of a credit bonanza.

Might it be interest rates? The OECD has suggested that rates in the UK should move up to 3.5 per cent by the end of next year to stamp out inflation. I don't think that is particularly likely – Mervyn King, Bank of England governor, has made clear that he will keep rates low to support the Con-Lib coalition as it cuts spending.

But what if rates did rise? Right now the average standard variable rate offered by most banks is about 4.5 per cent. A 3 per cent rise in rates (from the current 0.5 per cent) would take that up to 7.5 per cent. That wouldn't exactly push up demand.

But we don't necessarily need rising interest rates for mortgage rates to go up again. All we need is another interbank trust-leeching global crisis – like the one in Europe, perhaps. Note that Libor – the rate at which banks lend to each other and the rate from which many price their mortgages – has been creeping up again as risk aversion kicks in across the eurozone. The rise so far has been pretty modest relative to that seen during the Lehman Brothers collapse, but if panic sets in, it might not stay that way.

Other triggers might include falling real wages and an expected rise in unemployment as the government slashes its way through the public sector and rising taxes do for more service businesses.

There is also a new entrant into the mix: the coming rise in capital gains tax. We don't know how high this will go, but most people with a second home or a buy-to-let investment are likely to face a much higher tax bill on their gains than they had expected. That means they are probably running the numbers on selling right now.

A house bought for £100,000 in 1985 would now be worth £490,600 on Nationwide numbers. Sell it today and you'll pay CGT of £68,500. Sell it at 40 per cent and, assuming no inflation allowances, you'll pay £152,200. That suggests you should get out now – even if you can only do so at below what you think the market price should be.

Sell the £490,600 house today for £450,000 and you'll still clear more post-tax than if you waited and sold at 40 per cent. Even my mother is at it – her buy-to-let properties are joining the glut coming on to the market this week.

So, all in all, I'm not holding out much hope that our much-loved new townhouse will make our fortune.

However, if you insist on

buying, there is one thing I would recommend: do as we did and use a good search agent. It strikes me as very odd indeed that people go into a market in which they are not expert and spend hundreds of thousands of pounds, even millions of pounds, without taking advice from someone with their interests at heart (ie not an estate agent). A search agent will know houses are

coming on the market long before they hit primelocation.com.

Given that the property business is a magnet for charlatans, take recommendations on search agents where possible – we used Saint Property in Scotland.

Good agents will pay for themselves several times over. Ours did – which at least means we will lose less money on our

purchase than we might have otherwise.

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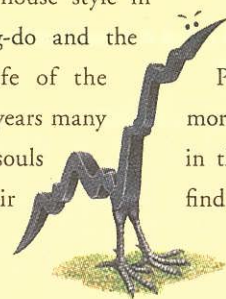


Fig.1: A typical PROFIT


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