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A rare breed: Home buyer balks at a $500,000 mortgage

By Rob Carrick

Meet Frank, who's squeamish about spending that much money in the current Toronto real estate market – even though he and his wife are supposed to be able to afford it

Debt does not rest lightly on his shoulders.

That's why a guy we'll just call Frank is having a tough time in the current Toronto real estate market. He figures he'll have to borrow upward of half a million dollars, and he's freaking out.

"It's a death sentence," said the 35-year-old husband and father of a young child. All three are living in a 700-square-foot downtown condo, and Frank says they need to move. "My wife wants more space, now, and she doesn't really care how we get it."

Frank's an engineer and his wife is an office administrator. They make good money, they've got no debt other than their condo mortgage and they've put together a down payment of $125,000. The bank says buying a $700,000 house is no problem for them, but Frank is squeamish about spending that much money. For the past three years, he's been saving with a goal of spending $500,000 on a starter home.

"The problem is that over the past two or three years, while we've been saving our down payment, the half-million-dollar starter home became a three-quarters-of-a-million-dollar starter home."

Canada needs more Franks – people who take a skeptical to paranoid view of debt. We'd have a more affordable housing market, lower household debt levels and less vulnerability to rising interest rates. We'd be both healthier as a country, and quite possibly wealthier.

But you can't easily opt out of taking on big debts. If everyone else in Toronto is willing to keep bidding house prices higher, then what's a guy like Frank supposed to do if he wants a house for his family?

Oddly, buying does make some sense for this high earner. Rona Birenbaum, a financial planner at Caring for Clients, did a quick analysis of his situation and found that a $550,000 mortgage plus various other basic housing costs would eat up about 25 per cent of his pretax household income. That's well below the 32-per-cent threshold the banks use for affordability. Bottom line, Frank and his wife would be able to carry a mortgage, save a reasonable amount and spend money on other things.

Ms. Birenbaum figures Frank's mortgage payments would rise about $600 a month if he renewed in five years and interest rates went up two percentage points. Taking Frank at his word that his family lives frugally, she said he'd still be okay.

She does have a few provisos for Frank, one being that the cost of daycare for a second child could squeeze his family's budget. Another is that he should plan to stay in the house he buys for the long term, rather than moving to something larger after just a few years. If Frank stays put, he won't have to worry about the possibility that prices could fall in the near term.

"If you're going to own real estate in Toronto for the next 20 or 30 years, then we're not at the high end of the market now," Ms. Birenbaum said.

Frank has considered taking an intermediate step of moving to a larger condo, but he's put off by his recent experience with condo fees. Pay attention if you've been considering buying a condo because these numbers are scary.

According to Frank, his condo fees have risen 5 per cent, 7 per cent, 13.5 per cent, 9.5 per cent and 6 per cent a year over the past five years, respectively. "Since I've been in my condo, the yearly increases in fees are way beyond inflation."

That leaves renting, which Frank is open to. But he recognizes that finding a suitable property will be hard in Toronto's tight rental market, and he doesn't want to be locked into a lease in case there's a big downturn in house prices.

If he buys, Frank would like to save up a bigger down payment and thereby reduce the amount he has to borrow. He suggested the idea of suspending contributions to his registered retirement savings plan to build up his down payment, and Ms. Birenbaum said that would be fine over a period of two or three years, max.

But here's the problem: Prices in Toronto jumped in August, and so did mortgage rates. Ms. Birenbaum's take on buying is that sooner is better than later.

What should Frank do? That question is posed on my Facebook personal finance page and I expect a lively debate. My thought is to take the renting option as far as it will go and, if that doesn't work, accept the inevitability of a big mortgage debt.

It sounds like Frank is already questioning whether his aversion to debt is working against him. "Inevitably, you're at the will of the masses," he said. "And if the masses are going to jump and make a horrible mistake, you're almost forced to do it as well."

What should Frank do?

- 1. Suck it up and buy a house already.
- 2. Buy a larger condo that has more space for his family, but costs less than a house.
- 3. Just say no to the housing market and rent.

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References

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