

COMPOUND INTEREST

INVESTIGATION

RENT OR BUY?

Although many dream to own their own home, the option of renting may be more financially viable, particularly if the purchase of a home is only for a short period (for example, 3 or 4 years).

CONSIDER THE FOLLOWING SCENARIO...

The Ling family has just moved from the USA. They plan to stay in the UK for only 3 years, after which time Mr Ling will receive a transfer to his company's overseas office. Should they purchase a house, knowing that they will have to sell in 3 years' time, or should they simply rent for the 3 years?

Mr. Ling has jotted down costs associated with purchasing and renting. These are itemized below.



PURCHASING

- Consider purchasing a home for \$300 000.
- Savings to be used for the purchase are \$35 000.
- Purchase expenses of \$5300 are to be allowed. This money will come from savings.
- Remaining \$ 29 700 provides the deposit for the housing loan.
- Repayments on the \$270 300 home loan are \$1942.89 per month.
- House maintenance costs (maintenance, rates and insurance) estimated to be \$4800 per year.
- Say the house sells for \$370 000 in 3 years' time.
- Real estate sale costs estimated at \$9700.
- Estimate the balance owing on the loan after the sale to be \$247 000.

RENTING

- Estimated rent on a house valued at \$3000 000 is:
- \$275 per week for the first year
- \$290 per week for the second year
- \$310 per week for the third year

- Invest the \$35 000 savings in a term deposit for 3 years at 6.2% p.a. compounding monthly.
- An extra \$10000 can be saved each year since rent costs are lower than house repayments. This money can be invested at the end of each year at 5.1% p.a. compounding monthly.

YOUR TASK

Q1. Draw up a schedule detailing the costs associated with buying and renting over the 3-year period. Show all calculations.

Q2. Write a report to Mr and Mrs Ling recommending whether they should buy or rent. Support your decision by referring to figures in your spreadsheet.

Q3. The Ling family has considered buying a house for \$300 000. How will the option to rent or buy change with the cost of the house? Give your assumptions and justify your answer.