Take the time to plan before taking the step to home ownership. - 123RF Stock Photo

Preparing for homeownership

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The affordability of rental units and new homes can be a challenge for many in Atlantic Canada, especially in areas where the costs of both is on the rise.

Even so, there comes a point where renters leave that market and move into homeownership. But at what point does it make financial sense to do so?

"It's when they're really financially ready. When they've really taken the time to plan for it and financially prepare for it," said Emily Rae, senior financial planning advisor with Assante Capital Management Ltd. in Halifax.

"And, to not get a mortgage with the most money you could possibly qualify for."

When approached by clients that want to make the jump to homeownership, she reminds them about the costs in addition to mortgage payments, such as property taxes and heating costs, and to keep an eye on where the housing market is, so they don't buy a property at the top of the market and then take a loss down the road.

Rae also advises clients to try and qualify or plan for a mortgage based on one person's income.

"For one thing, you won't be stretched too thin if you do that, or if somebody has an unexpected layoff or a period of time out of work due to maternity leave, that type of thing," she said.

In terms of whether your monthly rental is affordable, one way to look at it is using the Canadian Mortgage and Housing Corporation's affordable housing formula. The formula is annual shelter costs divided by annual income before taxes. If households are spending more than 30 per cent on shelter, they are not meeting the standard.

Statistics Canada recently published average weekly earnings for individuals in Canadian provinces (seasonally adjusted). So, for P.E.I., the average weekly earnings for an employed person for June was $834.19, or $3,614.82 for the month. Thirty percent of that monthly figure results in $1,084 as an affordable rent on the Island.

With respect to the other Atlantic Canadian provinces, 30 per cent of average monthly earnings in New Brunswick results in an affordable rent of $1,174 while in Nova Scotia it was $1,133.62 and Newfoundland and Labrador, $1,378.26.

A search of online apartment listings in Charlottetown shows that (depending on whether utilities are included or if furnished) prices can range from $900 to $1,750 per month for a twobedroom apartment. This range is an increase from a CMHC report that showed the average rental price of a two-bedroom apartment on P.E.I. in 2017 was $880 a month.

As well, the average price of homes on the Island has also increased – to $212,654 in August (a 5.1 per cent increase from August 2017) and increased by 4.7 per cent year-to-date to $211,024 compared to the same time period last year, according to the Canadian Real Estate Association.

Kim Reddin, owner and broker at CENTUM Mortgage Partners Inc. in Charlottetown, works with clients that want to make the jump from renter to homeowner and help them determine what they can afford. She explained that one calculation that has to be met is the Gross Debt Service Ratio, which determines whether the mortgage payment, property taxes and heating costs are less than 35 per cent of the applicant's before-tax monthly income.

The other calculation – Total Debt Service Ratio – involves mortgage payment, property taxes and other debt, such as car loans and credit cards. That total number can't be more than 42 per cent of a person's before-tax monthly income.

In the case of an applicant that is paying $1,200 a month in a rental, assuming that person has a five-per-cent down payment and good credit, that monthly rent would be nearly the same ($1,233.20 not including heat) as the mortgage payment on a $250,000 house. Even so, Reddin explained banks apply a stress test to make sure the applicant can afford a mortgage with an interest rate of 5.34 per cent (the Bank of Canada's five-year conventional mortgage rate) above the bank's rate of (on average) 3.5 per cent. This raises the $1,233.20 mortgage payment to $1,484, which lets the bank know the applicant can afford the higher payment in cases that the interest rate rises.

Rae notes that one option to help applicants cover the five-per-cent down payment is the Home Buyers' Plan that allows first-time buyers to withdraw and use money from their RRSP. Once the house is bought, she advises trying to make larger mortgage payments if possible in order to have it paid off quicker.

Rae added that she isn't opposed to renting an apartment.

"You don't have property taxes. You don't have to repair your roof. You don't have to put on a new deck. Usually all the fees are included," she said.

"We're told in our society that you should buy a house and that you're missing out if don't buy a house. But oftentimes I see people, perhaps, going into homeownership without having the nest egg."