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A new way to owning a home

A recently launched product, Rent2Buy, says it can open the door to home ownership if you're battling to save up for a deposit, particularly if your credit score is low. **Mark Bechard** looks at how it works.

Getting a foothold in the property market is a challenge for many middle-income people. They earn "too much" to qualify for the government's Flisp subsidy, but earn "too little" to manage a deposit of between 15 and 20 percent of the purchase price, as well as the costs, such as conveyancing fees, associated with buying a property. They may be paying rent – which could be consuming about a third of their monthly income – and have debts to repay. As a result, there's little, if any, money left over to set aside for saving for a property.

Over-indebtedness also sabotages the dream of owning a home; the banks do not look favourably on borrowers with a poor credit record.

Meyer de Waal, the director of a Cape Town law firm that bears his name, has developed a product called Rent2Buy that, he believes, addresses these obstacles to home ownership.

Essentially, Rent2Buy "freezes" the purchase price (plus a so-called option fee) of the property you want to buy – for two years. This provides you with time to get your financial house in order, which increases the likelihood that you will qualify for a home loan.

De Waal says Rent2Buy is aimed at people who:

- Have not been granted a 100-percent home loan and need to save for a deposit;
- Have minor problems on their credit status, such as arrears on accounts that can be settled within six months; and/or
- Need to improve their credit score.

The original concept – or Rent2Buy Standard as it's now called – was launched in 2007, but it failed to gain traction for a simple reason: most sellers cannot afford to wait for one, two or three years to receive all the proceeds from the sale of their property; they need the money immediately to finance the purchase of their next home.

To overcome this problem, De Waal last year launched R2B Finance, where a finance company buys the property outright as a cash sale. De Waal believes this new approach will greatly expand the pool of potential sellers. You, the prospective buyer, rent the property from the finance company for two years, and then:

- Apply to convert the rental agreement into an instalment sale and pay off the property over 20 years; or
- Obtains a mortgage bond from a bank or SA Home Loans; or
- If your application for both an instalment sale and a mortgage bond is turned down, you buy the property from



Rent2Buy for the original purchase price plus the option fee and sell it simultaneously to a new buyer.

Meeting the criteria

Rent2Buy Finance has a number of components – with accompanying obligations and costs. At the outset, it must be pointed out Rent2Buy does not guarantee that you will end up owning a home at the end of the two-year rental term. However, De Waal says, if you ensure that your credit record does not deteriorate during the rental period and have a good payment track record, it is likely that you will obtain approval for an instalment sale transaction or a mortgage bond.

To mitigate the risks to both parties, you have to meet the following pre-qualification criteria:

- The ability to put down a deposit of about seven percent of the purchase price if you buy from a private seller, or between three and five percent if you buy from a developer.
- Any blemishes on your credit record, such as accounts in arrears, must be able to be removed within six months.
- You must be able to afford the monthly rental. Rent2Buy will provide you with a quote after it conducts an affordability analysis.
- You must be able to afford the costs associated with owning a home, such as rates and insurance.
- Your overall financial situation must be such that, within two years, it is likely you will qualify for an instalment sale or a mortgage bond.

Rent2Buy will thoroughly check your financial situation to ascertain whether you meet these criteria. The pre-qualification process costs R750, plus R100 for each co-purchaser, such as your spouse.

If your finances pass muster, you will be issued with a certificate of affordability, which entitles you to look for a home, currently only in the Cape Town metropolitan area and Gauteng. The certificate is valid for three months. The property cannot have a purchase price of more than R1.8 million or less than R400 000.

Once you find a property you want to buy, you put in an offer, which, De Waal says, should be made subject to obtaining a 100-percent home loan. This condition will protect you if Rent2Buy does not approve the valuation of the property. (At this stage you can still apply for a loan from a bank.)

If the seller accepts your offer, you inform Rent2Buy, which will step in and negotiate to take over the purchase of the property as a cash sale, subject to an acceptable valuation. If Rent2Buy is satisfied with the property's risk profile and pricing, it will take transfer of the property.

You will enter into two contracts with Rent2Buy: a lease agreement to rent the property for two years and an agreement containing an option to buy the property when the lease expires. You have only the right of occupation during the two-year period. If you do not pay the rent and fail to remedy the breach, the agreements will be terminated and you will be evicted.

A further condition is that you enrol in My Budget Fitness, a programme that, over two years, aims to help you improve your financial situation and credit score so that it is more likely that you will be granted a home loan. The programme, which includes a budgeting app, educates you about homeownership, financial management, and how to apply for a home loan and negotiate the best interest rate. The My Budget Fitness fee is R150 a month, or R3 600 over the two-year term.

Rent2Buy will "stress-test" your credit score and finances every four months to see how you are progressing towards becoming home loan-ready.

Crunching the numbers

As stated above, you need to put down a deposit of up to seven percent of the purchase price. Let's say the home you want to buy costs R1.8m. A seven-percent deposit means you will have to put down R126 000. Rent2Buy uses this amount to cover the conveyancing costs, the rental deposit, and the option fee.

De Waal says the conveyancing fees on a R1.8m property will be about R28 600. If the sale is subject to transfer duty, you will not have to pay this duty; the cost will be absorbed by the finance company, which

is a registered VAT vendor. If the seller is not registered for VAT – which is normally the case with private sellers – the company will effectively be able to claim back the transfer duty as a VAT input after the sale has been registered. In this case, not having a pay transfer duty has saved you R44 500.

Then there is the rental deposit, which is twice the monthly rental.

Rent2Buy charges rental at 2.75 percentage points above the prime lending rate, which is currently 10.25 percent. The 2.75-percentage point spread is fixed throughout the two-year term.

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On a R1.8m property, De Waal says the rental, plus the premium for mandatory rental guarantee insurance, plus the My Budget Fitness fee will come to R21 435 a month (a total of R514 440 over two years).

Therefore, the rental deposit will be R42 870. This money will be refunded to you at the end of the two-year term, less deductions, if any, to cover damage to the property.

None of the rental you pay over the two years is offset against the purchase price.

The balance of the R126 000, or R54 530, is the option fee, which Rent2Buy will retain for the two-year term. It will be refunded to you at the end of the term if you adhere to the agreement and buy the property via an instalment sale or a mortgage bond.

The upfront seven-percent deposit is not all you will pay. During the two years you rent the property, you will be liable for

the costs associated with owning a home, including municipal rates and services, and maintenance and repairs. De Waal says the reason for this is to test whether you can afford the expenses that come with home ownership.

From renting to buying

Shortly before the two-year rental term is due to expire, De Waal says you can apply to convert the lease to an instalment sale. Whether your application will be granted depends on your financial behaviour over the past two years. If your application succeeds, you will buy the property from Rent2Buy Finance for the purchase price plus the option fee. However, the option fee is credited to you as "a down payment".

De Waal says the term of the instalment sale, which is governed by the National Credit Act, is 240 months, or 20 years.

You will not have to pay transfer duty if the purchase price is more than R900 000, because the sale will be subject to VAT, which is included in the purchase price.

He says the interest rate is calculated at prime plus 2.75 percent, unless your credit profile deteriorated while you were renting the property, in which case you will pay a higher rate. As with a normal home loan, the interest you pay is calculated monthly based on the total amount outstanding to the end of the 20-year term.

De Waal says are you charged the following fees for an instalment sale:

- A fee of about R3 800 plus VAT to register the instalment sale agreement against the title deed in the Deeds Office;
- An upfront commencement fee of up to one percent of the loan amount, capped at R5 985 plus VAT; and
- Conveyancing fees at the end of instalment period, to register the property in your name.

If Rent2buy Finance declines your application for an instalment sale, you can either obtain a mortgage bond or

put the property up for sale, at a market-related price, and find a buyer. De Waal says that, once you find a buyer, you buy the property from Rent2Buy Finance and, in a simultaneous registration process at the Deeds Office, pass transfer to the new buyer. You will retain any profit made on the transaction. However, you will forfeit the option fee.

Some observations

The main selling point of Rent2Buy Finance is that the purchase price increases by the option fee and is then frozen for two years, which means that you aren't chasing a moving target while trying to save for a deposit. However, to compensate Rent2Buy for holding the property for two years, you pay rental based on prime-plus-2.75 percent of the purchase price, instead of one determined by market forces.

Whether this works in your favour depends on how much more you could ending up paying for the property in two

years' time if the price were not frozen. It is therefore in your interest to do your research and find out how property prices are appreciating in the area in which you want to buy. According to First National Bank's Property Barometer for February 2018, property prices in Cape Town grew by an average of 10.8 percent year-on-year in the fourth quarter of last year, and by 2.4 percent in Gauteng. These headline figures obscure the price-growth differences among specific suburbs and areas. Unfortunately, property price statistics are backward-looking, so you can't know for certain whether, or for how long, a trend will continue.

Another selling point of Rent2Buy is that you save on transfer duty. However, this saving applies only if the property you want to buy sells for more than the transfer duty threshold of R900 000.

