Making affordability work: How builder incentives help buyers get into new homes

BY TIM MURPHY
NORTH STATE BUILDING INDUSTRY ASSOCIATION

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Ask prospective homebuyers about the biggest challenge they face today, and you'll probably hear the same answer: affordability.

Higher mortgage interest rates have certainly made buying a home more expensive, but they are only part of the equation. The cost of land, labor and building materials has increased significantly in recent years. Government fees and regulatory costs now average more than $100,000 on every new home built in the Sacramento region. Together, those factors have pushed the price of housing beyond the reach of many families.

Homebuilders can't control most of those costs. They can't set interest rates, reduce permit fees or eliminate regulations that add thousands of dollars to every home.

What they can do is find creative ways to help buyers overcome today's affordability challenges. And that's exactly what many builders are doing.

The most visible example is mortgage rate buydowns. Working with preferred lenders, builders often subsidize interest rates, allowing qualified buyers to finance a home at rates well below current market levels. Depending on the community and the promotion, those lower rates may apply during the first year or two of the loan or even for its full term.

At first glance, some buyers might wonder why builders don't simply lower the home's price instead.

The answer is surprisingly simple: lowering the monthly payment usually provides much more value.

Consider a buyer financing a $500,000 mortgage. A two-percentage-point reduction in the interest rate can lower the monthly payment by hundreds of dollars. Over the first several years of the loan, those savings can easily exceed the benefit of a modest reduction in the purchase price.

That's why financing incentives have become such an effective affordability tool. They help buyers qualify for a loan, make

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monthly budgeting easier and preserve the home's long-term value. Simply cutting the sales price has a much smaller effect on the monthly payment while also influencing future appraisals and comparable sales throughout a neighborhood.

Financing, however, is only one item in builders' affordability toolbox.

Many builders are also paying some or all of buyers' closing costs, offering credits toward upgraded flooring, countertops and appliances, including smart-home technology, or waiving lot premiums. Buyers shopping for quick move-in homes often find additional incentives as builders work to sell completed inventory and begin construction on the next phase of a community.

Taken together, these incentives can reduce both the cash needed at closing and the ongoing monthly cost of homeownership. For many buyers, that's the difference between continuing to rent and finally purchasing a home.

Of course, incentives are not a permanent solution to California's affordability challenges. While current interest rates are historically about average, affordability could be greatly enhanced by reducing the cost of producing housing in the first place.

That means addressing excessive government fees, streamlining the permitting process and removing unnecessary regulatory barriers that make every new home more expensive before construction even begins.

Until those reforms occur, builder incentives are helping bridge the gap. They don't eliminate the affordability challenge, but they are making homeownership possible for many families who otherwise might believe buying a new home is out of reach.

So if you've considered buying a new home but haven't thought it was possible, take a look at some of the 200 new home communities in our region and talk to a few builders. You may find that the home of your dreams is more affordable than you think.

Tim Murphy is President & CEO of the North State Building Industry Association, which represents builders, developers, subcontractors, suppliers and related professionals dedicated to providing new housing opportunities in the Greater Sacramento region.