Rent Vs Buy

When we acquire a lump sum of money, we frequently get unsure of what to do—should we invest it, or should we use it to purchase a home? Do I receive any tax benefits? How does inflation play a role in all of this? Do I need to think about inflation or not? How can I be sure that my money will increase at what pace if I invest?

Here we are, trying to explain to you all these points based on a hypothetical example that can relatable to a real-life situation to understand the rationale thinking behind these two options Rent or Buy.

Scenario 1: We have a lumpsum amount of 40,00,000 used as a downpayment vs renting a property.

Assumption The "Basic Salary" refers to the amount of money earned before any taxes or deductions are taken out. In this case, the Basic Salary is 8,00,000.

Comparison between Buying and Renting of House				
Purchase of Property			**Renting Property**	
Purchase price	50,00,000		Rental Inflation	10%
(a) Downpayment	**40,00,000**			
Loan amount	10,00,000		Assumed Market Returns on MF Investment	12%
Home loan interest rate	8.00%			
Monthly EMI for 15 years	**9,557**			
			B. Monthly Renting	
(b) Total amount paid over 15 years	**17,20,174**		Monthly rent	35,000
			HRA Tax benefit	8,500
Property maintenance (Monthly)	2,000		Net monthly rent	26,500
Maintenance inflation	10%		Annual rent	3,18,000
(c) Total Maintenance paid over 15 Years	7,62,540		Rental inflation	10%
			Maintenance	**7,62,540**
Total Outflow over 15 years (a+b+c)	**64,82,713**			
Total Outflow 15 years	64,82,713		Total Outflow after considering tax benefit	1,08,66,189
Future value of the property after 15 years	1,58,60,846		Mutual Fund Investment Inflow	2,39,83,208
Tax saved over 15 years	7,97,907			
Net Inflow	**1,01,76,040**		**Net Inflow**	**1,31,17,019**

The "Tax Bracket" indicates the percentage of income that will be paid in taxes. In this case, the tax bracket is 30%.

The table compares the financial implications of buying and renting a property over a period of 15 years. It compares the total amount paid for buying a property with a purchase price of 50,00,000 and making a down payment of 40,00,000 with the monthly rental expenses of a property with a monthly rent of 35,000.

Under the "Purchase of Property" section, the table shows that the purchase price of the property is 50,00,000. A down payment of 40,00,000 is made, and the remaining amount of 10,00,000 is taken as a home loan with an interest rate of 8% (As home loans are attached to interest rate, we took a fixed interest rate for our calculations). The monthly EMI for a home loan for 15 years will be 9,557 and the monthly maintenance cost for the property is assumed to be 2,000, with an assumed annual maintenance inflation rate of 10%. The total amount paid over 15 years against the home loan is 17,20,174, and the total maintenance paid over 15 years is 7,62,540. The total outflow over 15 years, including the cost of the property, home loan EMIs, and maintenance cost, is 64,82,713. The future value of the property after 15 years is assumed to be 1,58,60,846. The tax saved for 15 years due to home loan interest payment is 7,97,907. The net inflow after selling the property and paying off the home loan, which is the future value of the property minus the total amount paid over 15 years and the tax saved, is 1,01,76,040.

Under the "Renting Property" section, the table shows that the monthly rent for the property is 35,000. An assumed annual rental inflation rate of 10% is considered. The HRA tax benefit is assumed to be 8,500, which is adjusted against the monthly rent of 35,000 to arrive at a net monthly rent of 26,500. The annual rent paid is 3,18,000 and maintenance is the same as under "Purchase of Property" i.e. 7,62,540. The total outflow over 15 years after considering the HRA tax benefit is 1,08,66,189. The assumed market return on mutual fund investment is 12% and have invested 40,00,000 as lumpsum money. The mutual fund investment inflow after 15 years will be 2,39,83,208. The net inflow after 15 years, which is the mutual fund investment inflow minus the total outflow over 15 years after considering the HRA tax benefit and maintenance cost, is 1,31,17,019.

	Purchase of property	**Renting property**
Net Inflow	1,01,76,040	1,31,17,019

It is clear from the above table that renting a property is better than purchasing property as One will receive an extra benefit of 29,40,979.

Scenario 2: Except downpayment of 40,00,000 what if we made a down payment of 10,00,000 to buy a property vs renting a property?

Assumption The "Basic Salary" refers to the amount of money earned before any taxes or deductions are taken out. In this case, the Basic Salary is 8,00,000.

The "Tax Bracket" indicates the percentage of income that will be paid in taxes. In this case, the tax bracket is 30%.

Comparison between Buying and Renting of House				
Purchase of Property			**Renting Property**	
Purchase price	50,00,000		Rental Inflation	10%
(a) Downpayment	10,00,000			
Loan amount	40,00,000		Assumed Market Returns on MF Investment	12%
Home loan interest rate	8.00%			
Monthly EMI for 15 years	**38,226**			
			B. Monthly Renting	
(b) Total amount paid over 15 years against home loan	**68,80,695**		Monthly rent	35,000
			HRA Tax benefit	8,500
Property maintenance (Monthly)	2,000		Net monthly rent	26,500
Maintenance inflation	10%		Annual rent	3,18,000
(c) Total Maintenance paid over 15 Years	7,62,540		Rental inflation	10%
			Maintenance	**7,62,540**
Total Outflow over 15 years (a+b+c)	**86,43,235**			
Total Outflow 15 years	86,43,235		Total Outflow after considering tax benefit	1,08,66,189
Future value of the property after 15 years	1,58,60,846		Mutual Fund Investment Inflow	61,67,560
Tax saved over 15 years	22,19,488			
Net Inflow	**94,37,099**		**Net Inflow**	**-46,98,629**

This table compares the total amount paid for buying a property with a purchase price of 50,00,000 and making a down payment of 10,00,000 with the monthly rental expenses of a property with a monthly rent of 35,000.

Under the "Purchase of Property" section, the table shows that the purchase price of the property is 50,00,000. A down payment of 10,00,000 is made, and the remaining amount of 10,00,000 is taken as a home loan with an interest rate of 8%. The monthly EMI for the home loan for 15 years will be 38,226 and the monthly maintenance cost for the property is assumed to be 2,000, with an assumed annual maintenance inflation rate of 10%. The total amount paid over 15 years against the home loan is 68,80,695, and the total maintenance paid over 15 years is 7,62,540. The total outflow over 15 years, including the cost of the property, home loan EMIs, and maintenance cost, is 86,43,235. The future value of the property after 15 years is assumed to be 1,58,60,846. The tax saved during 15 years due to home loan interest payments is 22,19,488. The net inflow after selling the property and paying off the home loan, which is the future value of the property minus the total amount paid over 15 years and the tax saved, is 94,37,099.

Under the "Renting Property" section, the table shows that the monthly rent for the property is 35,000. An assumed annual rental inflation rate of 10% is considered. The HRA tax benefit is assumed to be 8,500, which is adjusted against the monthly rent of 35,000 to arrive at a net monthly rent of 26,500. The annual rent paid is 3,18,000 and maintenance is the same as under "Purchase of Property" i.e. 7,62,540. The total outflow over 15 years after considering the HRA tax benefit is 1,08,66,189. The assumed market return on mutual fund investment is 12% and have invested 40,00,000 as lumpsum money. The mutual fund investment inflow after 15 years will be 61,67,560. The net inflow after 15 years, which is the mutual fund investment inflow minus the total outflow over 15 years after considering the HRA tax benefit and maintenance cost, is 1,31,17,019.

	Purchase of property	**Renting property**
Net Inflow	94,37,099	-46,98,629

It is clear from the above table that buying a property is better than renting a property as One will receive an extra benefit of 1,41,35,728.

The conclusion from the above two scenarios:

We can determine the break-even point at which one can assess the lump sum amount and at what value one can make an intelligent decision. Investors are encouraged to rent a home rather than purchase one of their lump sum is greater than 70.13 percent, roughly. If the lump payment is less than approximately 70.13%, consider purchasing a property. Therefore, it is advised to young investors who are growing their wealth to buy a house in the beginning when they have a lumpsum amount below 70% of the property as it gives more wealth to the investor. Not just this, it also gives investors emotional support that they own an asset that can help them during tough times by liquidating it.

Note:

- The above calculations are shown based on a rental yield of 8.4% of the current market value.
- Annual Rental increment is 10%.
- Investor is in the tax bracket of 30%.
- Maintenance of the property is 0.04% of the current market value of the property.

Research Desk

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