

AN OVERVIEW FOR PROSPECTIVE HOMEBUYERS

WHY OWN A HOME?

Homeownership is part of the American dream. For most Americans, buying a home is the single largest purchase made in their lifetime. Owning a home provides shelter and is also an investment. It is an asset that you can use to finance education expenses or pass along to your children. Additionally, the initial source of equity for many small businesses is a second mortgage on a home. Homeownership gives you a real stake in the community and serves to empowering individuals and families to promote positive neighborhood change. Paying rent does not build your personal wealth – it enriches your landlord. However, as you make payments to reduce the mortgage on your home, the equity in your home is increased. This increase in equity as well as any appreciation in the market value of your home increases your personal wealth.

Searching for a home and obtaining mortgage financing can be a daunting process. Here a few questions frequently asked by prospective homeowners that you can use for reference as you take the initial steps toward becoming a homeowner.

HOW MUCH CAN YOU AFFORD TO PAY FOR A HOME?

As a general rule of thumb, you should be able to afford to purchase a home that costs in the range of 200% to 250% of your annual gross income, i.e., if your annual gross household income is \$50,000 you should be able to purchase a home priced at \$100,000 to \$125,500.

HOW CAN YOU DETERMINE IF YOUR INCOME IS SUFFICIENT TO PURCHASE A PARTICULAR HOME?

In order to determine if your income is sufficient to purchase a particular home, consideration must be given to your living expenses as well as to certain criteria lending institutions use to evaluate your application and determine the maximum loan that you can likely afford. These criteria are generally referred to as the Front-end Ratio and the Back-end Ratio. The Front-end Ratio relates to your housing expenses (mortgage payments, property taxes and insurance fees, co-op maintenance, condominium carrying charges, etc.). In general, depending on the lending institution and the mortgage product, not more than 28% to 33% of your gross household income should be devoted to housing expenses. The Back-end Ratio relates to your housing expenses plus other consumer debt such as credit cards, student loans, car loans and personal loans. In general, not more than 36% to 38% of your gross household income should be devoted to the combination of housing expenses and consumer debt.

HOW MUCH CASH WILL YOU NEED TO PURCHASE A HOME?

The amount of cash that you will need to purchase a home is in part based on the purchase price of the home you are seeking to purchase and the amount of financing that you can obtain from a lending institution. The minimum down payment can be as low as 3% or as high as 20% depending on the mortgage lender, the proposed property and its purchase price. There are also loan products that offer 100% financing, i.e., 0% down payment. While shopping for a mortgage, you should inquire about the availability of and qualifying criteria for these 0% down payment mortgages. In addition to the down payment, you will also have to pay closing costs. Closing costs include various fees and expenses such as mortgage recording tax, legal fees, title fees, etc. and generally range from 4% to 7% of the loan amount. The down payment is due upon signing a contract; closing costs are due at closing on your mortgage loan.

HOW CAN YOU DETERMINE IF YOUR CREDIT IS EXCELLENT, GOOD OR POOR?

Lending institutions will review your income, assets, employment history and credit history in determining if you qualify for a mortgage loan. Your credit history is an important factor in obtaining approval for a loan. In order to avoid any last minute surprises, you should obtain a copy of your credit report and review it prior to applying for a mortgage. Any inaccurate information that is contained on your credit report should be brought to the attention of the credit reporting agency, in writing. If there is unfavorable but accurate information you should take steps to address these matters. Additionally you should be prepared to provide a mortgage lender with a written explanation of the problem(s) that caused the negative credit and what measures you have taken to ensure that it does not recur. You can obtain a copy of your credit report from Equifax Informational Services (800-378-2732), Experian Informational Services (888-397-3742) and/or Trans Union Corporation (800-888-4213).

