

What You Can Afford . . .

When applying for a home loan, personal finances should be your first concern. Your income versus your debt will likely determine the amount a lender will allow you to borrow.

- 1. The first step is to determine your *gross* monthly income.** This includes any regular and recurring income that can be documented. If you cannot document the income, or if it does not appear on your tax return, then you probably cannot use it to qualify for a loan. You can, however, use unearned income, such as alimony or lottery payoffs. If you own income-producing assets including real estate and stocks, that income can be used.
- 2. Next, determine your total monthly debt.** This includes credit cards, installment or car loans, alimony or child support, or any continuing monthly obligation. For credit cards, use the minimum monthly payment for calculation purposes. For installment loans, use the current monthly payment. Installment debt that is scheduled to be paid in full within the next ten months does not have to be considered. This total is sometimes referred to as “monthly debt service.”

Lenders will not allow you to borrow more than your ability to repay all of your obligations, especially your mortgage.

- 3. Your monthly housing expense including taxes and insurance should not exceed around 28% of your gross monthly income.** If you do not know exact figures, tax and insurance expenses can be estimated at 15% of your monthly housing payment. The remaining 85% is assigned as interest and principal.
- 4. In addition, your monthly housing expense plus your total monthly debt service cannot exceed 36% of your gross monthly income.** If you are not within this parameter, you may not fit the lender’s underwriting guidelines, and the lender may not approve your application.

Each individual borrower has a unique situation, and different lenders may be more or less flexible than the 28% and 36% suggested guidelines. If you are able to purchase a home by borrowing less than 80% of the home’s value – by making a large cash down payment, for example – then these guidelines may become less critical. Many different loan programs are available, all with different guidelines, so some may be more applicable to your financial situation. Your financial professional or loan officer can outline a program that best fits your needs, helping you to get the home of your dreams.