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## Determining How Much Home You Can Afford in a Credit-Crunched Market

If you are trying to break into the housing market today, you may face greater difficulty in securing mortgage funding than you might have a few years ago. The proliferation of bad loans made during the housing boom has led to a dramatic increase in foreclosures among subprime or poor credit borrowers. The resulting losses have scared many investors out of the secondary markets, creating a shortage of mortgage credit available to many home buyers. How much house you can afford in today's market is probably less than you could have qualified for a few years ago. Take a look at the following suggestions for determining how much you can afford.

### Using Ratios

Traditionally lenders have used the 28/36 ratio to figure out how much to lend you. That means your monthly mortgage payment including taxes and insurance should not total more than 28 percent of your monthly income in order for you to comfortably and safely repay the loan. Your total debt including your mortgage bill should not total more than 36 percent of your income.

During the housing boom, lenders often fudged on these ratios and let people slide by with higher percentages, counting on the rapidly inflating house prices to cover the difference. Now that home price appreciation has slowed and even reversed in some places, lenders are going back to stricter standards for mortgage applicants. Try to keep your ratio well within the 28/36 ratio.

### Can You Downsize Your Expectations?

"Borrowers should play it safe and stick to the old formula, even if it means scaling back expectations," said Christina Diaz-Malone, director of national initiatives at Freddie Mac. "You may need to start with a condominium or a cooperative. Look at your purchase as the first investment, and then move up."

That may not be your ideal plan, but in a down market it is safer to be conservative rather than extravagant in your purchases. You can get into something small now and ride out the down market, and then upgrade once you have accumulated some good equity.

### Do You Have Income Documentation?

Be prepared to provide plenty of income documentation to your lender. Without full documentation, you either be rejected for the amount of funding you are requesting or you will have to pay a significantly higher interest rate for the added risk.

### How Much is Your Down Payment?

The size of your down payment will also determine how much money you can borrow. Do not think you can still get away with putting zero money down in the current market. With tighter credit, you will be expected to contribute something to buy down the risk of the loan. With a larger down payment you may also be able to borrow a little more money as well.



### Shop Around

Once you figure out how much you should and could borrow, shop around among the various lenders to compare interest rates and terms. Be sure to do your research on different mortgage loans available – specifically the difference between fixed-rate and adjustable rate mortgages (ARMs.) Decide which one is best for you and that will make your loan comparisons much easier.

Remember, how much you can afford to pay for a house is not only a matter of finances, but also of lifestyle. Make sure the loan amount you apply for will be manageable and will fit in with your other life goals and fiscal pursuits.