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Proactive Loan Shopping May Save You From a Subprime Loan

Is there anything worse than that feeling you get when you realize you have paid way too much for something? Unfortunately for many American homeowners, they may be experiencing exactly that kind of remorse when it comes to their home loans. According to recent statements from Freddie Mac, a government-sponsored mortgage finance company, among the subprime loans it bought in 2005, as many as 15 to 35 percent of the loan borrowers could have actually qualified for a prime rate loan. Freddie Mac's sister company, Fannie Mae estimated that of the subprime loans it bought in 2005 perhaps 50 percent of the borrowers had credit scores high enough to get prime loans.

Let's put this discrepancy into perspective. Because subprime mortgages were created to service those with more risky credit backgrounds (scores of 650 or lower), subprime lenders charge higher interest rates and often more points to compensate for the greater risk. Typically a subprime loan will increase your interest rate by at least 3 percentage points or more what you would get with a prime loan. If you take out a $200,000 loan that means you will be paying an extra $300 a month to your mortgage bill, if not more. If you don't have to get one of these pricier loans, why would you?
Basically, you might accidentally get stuck into a subprime loan through sheer ignorance. According to a 1999 survey by the Mortgage Bankers Association, 31 percent of all home buyers never spoke to anyone else in the home buying/mortgage process but their real estate agent. "The survey needs to be updated," said Doug Duncan, chief economist for the MBA. "But it still suggests that many consumers enter some of the biggest financial deals of their lives with their eyes wide shut."

So if you want to avoid this problem, you have to take the responsibility for getting a good home loan into your own hands. You have already taken the first step by learning the difference between subprime and prime mortgage loans. Now you need to find out exactly what your credit score is and whether you could qualify for a prime loan. You can obtain your credit score for a small fee by visiting the website of any of the three major credit reporting agencies – Experian, Equifax, or TransUnion. With this information in hand, you be much less likely to get pushed into a subprime loan that you don't need by an unscrupulous mortgage lender. Find out what the going rates are for loans associated with credit scores like yours. This will give you more leverage in negotiating a good deal.

Another key to getting the best loan for your situation is shopping around. Don't just go with the lender that your real estate agent suggests. Do your homework and get quotes from several mortgage lenders. Start with prime lenders. If you repeatedly get rejected by prime loan lenders, you may in fact have to turn to a subprime loan. But you will never know if you could have qualified for a cheaper loan if you don't try!