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Affording a Home

When you feel its time to get into a new home, there are lots of factors to consider. The most important being “Can I afford to buy?” As simple as that sounds, it can actually be a very loaded question. You should do some preliminary research to make sure you know the answer.

The first issue at hand is to determine how much of your monthly budget you can put toward a mortgage payment. You need to consider all of your current debts, how much income you have now, and how much income you anticipate in the near future. Most lenders will take a look at your debt-to-income ratio to make a rough estimate of how much your monthly mortgage payment should be. The ratio is a percentage based on your total monthly debt, including mortgage installments, divided by your monthly gross income. A safe bet is to keep your debt down to about 30% of your monthly income (although some lenders will allow it to be up to 45% of your income.) To find out how much mortgage debt you can take on monthly, try this formula:

Gross Monthly Income ($)
X 0.30

Total Monthly Debt
- Non-Mortgage Debt

Allowable Mortgage Payment

In the formula above, the non-mortgage debt should include any credit card bills, student loans, car payments, monthly utility bills, and your monthly entertainment and travel expenditures. Once you’ve discovered how much you can pay each month in mortgage fees, you can move on to your next set of considerations.

Consider that the mortgage payment you calculated does not mean all the money will be going to the principal and interest of your loan. It will probably include your yearly property taxes (usually a percentage of your home’s worth) and also private mortgage insurance payments (if your down payment is less than 20% of the loan total.) This might mean that after figuring in the tax and insurance you may not be able to afford as much house as you thought.

Your calculations so far will be a preliminary figure to find out if and how much you can afford. When you actually sit down with a mortgage lender, however, he or she will use a much more specific and complex combination of variables to decide your ability to pay off a mortgage. Lenders will start by evaluating your current and future income potential. They will then pull your credit report and evaluate your history of making payments. (The better your credit score, the easier it will be to acquire a loan. Try to do everything you can to clean up your score before applying for a home loan.) Other considerations by lenders will include how much of a down payment you can contribute, the length of your proposed loan, your total amount of debt, the interest rate you’ll be paying on your mortgage, and also the probability that you’ll default on your loan payments. All of these factors together will determine the size of the loan you will be able to receive.

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However, just because you are offered a certain amount of money doesn’t mean that it is truly in your best interest to borrow that much. You have to decide what size payment is within your comfort zone. Don’t forget that there will be lots of associated costs with buying and owning a new home. Before you actually get into your home you may have to pay for realtor fees, a down payment, and closing costs. After the home sale, in addition to the mortgage payment, you might have to pay for homeowner’s insurance, new furniture or appliances, maintenance and upkeep of your new place and the cost of any repairs of remodeling you decide to do.

Buying a home is an exciting and sometimes overwhelming process. Taking a look at your financial status and all the potential fees before starting the application process will help you to feel secure in your ability to afford the purchase.

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