UNDERSTANDING MORTGAGES AND COSTS

SHOULD I GET PRE-APPROVED?

Being pre-approved gives you a big advantage. It improves your negotiating position by presenting you as a serious buyer, and can help you close on a property faster and with less stress. It also helps you determine a realistic budget. Jill Team can put you in touch with a loan officer or mortgage counselor, and can also suggest alternative ways to approach the down payment and financing.

HOW MUCH CAN I AFFORD?

A lender typically uses a 28% formula, meaning your monthly mortgage payment shouldn't exceed 28% of your monthly income, but there are other factors that are considered in a loan application. Only a qualified loan officer or counselor can give you a true picture of how much debt you might be approved for.

HOW DO MORTGAGES WORK?

Basic principles govern most mortgage loans:

The home is used as security to back the loan, meaning a lender can force the sale of the home if the borrower fails to make their scheduled payments.

The larger the loan compared to the value of the home, the more risky it is for the lender and, often, the more expensive the loan will be for the borrower.

Loans are divided into principle – the amount borrowed – and interest – a percentage of the principle that is charged by the lender. Interest is always equal to the periodic interest rate times the outstanding principle balance of the loan. The required monthly payment usually is a bit larger than the interest due so that some of the loan principal is repaid with each payment. This process is called amortization.

WHERE DO I GO FOR A MORTGAGE?

The modern mortgage market offers a variety of loans that cater to the needs of homebuyers. You can apply for a loan through a traditional bank, over the Internet, or even through a mortgage broker who will shop from hundreds of lenders. The details of these plans can be confusing, especially as new types are introduced. A qualified loan officer or mortgage counselor can help you make informed comparisons.

Jill Team
Jill Aldineh
(937) 303-1888
JillTeam.com

WHAT TYPES OF MORTGAGES ARE AVAILABLE?

As you learn more about the types of financing available, you will notice that some loans appear to have more favorable terms. That may indicate that those loans are, indeed, bargains (and it does pay to shop around), but usually it means that those loans could have some feature that is less appealing to borrowers. For example, shorter-term loans often have slightly lower interest rates compared to longer-term loans. However, the monthly payment for the same amount of principal may be higher because of the shorter term.

Fixed-rate mortgages are generally offered in 15- or 30-year terms and allow buyers to take out a long-term loan with either fixed payments or graduated payments over the course of the term

Adjustable-rate mortgages (ARMs) have an initial fixed rate (which may be lower than a comparable fixed-rate mortgage) but allow for rate adjustments over time based on the performance of key indexes. While the lower rates on ARMs may be appealing, the assumption that you will be able to pay higher rates down the road should be well thought through. ARMs have fallen out of favor recently, but they are still useful for buyers who will be selling their property in the short term.

FHA loans are backed by the government and can require as little as 3.5% down, but borrowers are required to purchase mortgage insurance, which will add to their monthly costs.

Additional loans are offered for first-time buyers and people in specific professions and income brackets.

WHAT ARE PRE-PAYMENT PENALTIES?

Pre-payment penalties are fees lenders can charge for paying off the principal of your loan early. If possible, try to avoid loans with prepayment penalties. Making extra payments on the *principal* of your loan as your budget allows can shorten your loan term and save you thousands of dollars in interest costs.

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