

Who Are the 7 Key Players in the Mortgage Market?

We like to think that people have made the home loan process so simple that you could easily get a mortgage and make payments on it for 30 years *without* having much of a clue as to where the money came from, how the interest rate was set and other inner-workings of the system that makes it possible for thousands of Americans to buy homes every year. With all the recent tumult in the lending industry, however, you have good reason to want to be informed about what's going on inside the magic mortgage market machine. So we've arranged a peek behind the curtain at who is pulling the levers. Here are the 7 key players in the mortgage market:

1. Mortgage lenders

Used to be you'd go down to your local bank office to discuss borrowing with a loan officer. Now, while banks are still big mortgage lenders, there are a slew of other firms whose only business is making loans.

2. Fannie Mae

The Federal National Mortgage Association (FNMA) was formed in 1938 to provide banks with federal money so they could make home loans during the Great Depression. In 1968 it was privatized, but as a government-sponsored enterprise (GSE). Fannie Mae was taken over by the Federal Government in late 2008.

3. Freddie Mac

Another GSE that was recently taken over by the Federal Government, the Federal Home Mortgage Corporation (FHMC) was formed by the federal government in 1970 so that Fannie Mae did not hold a monopoly on the secondary mortgage market, in which Fannie and Freddie buy mortgage



obligations from primary mortgage lenders (see #1). Together, Fannie and Freddie own more than half of all U.S. mortgage debt.

4. Investment banks

Along with Fannie and Freddie, investment banks are major buyers in the secondary mortgage market. Mortgage lenders use the cash they get from selling mortgages to make more mortgages.

5. Investors

Fannie, Freddie and investment banks bundle the mortgages they buy into "mortgage-backed securities," which are then sold to investors, who profit from the payments that borrowers make on the mortgages in the bundle. How much investors are willing to bid for mortgage-backed securities influences interest rates as well as the availability of home loans.

6. Federal Reserve

The Federal Reserve also influences the mortgage market because it sets the discount rate, or the amount banks charge one another for overnight loans. The discount rate plays an indirect role in determining mortgage rates.

7. U.S. Treasury

The Treasury Department supports Fannie Mae and Freddie Mac by making a line of credit available to them. Recently, Treasury officials have taken the unprecedented step of bringing Fannie and Freddie under federal control, after weakness in the housing and mortgage markets threatened to sink the two mortgage giants.

For more information or if we can answer any other questions you might have, contact our office today!

Home Buying Mistakes to Avoid at All Costs!

There are some common errors people make when buying a home. Be aware of the following home buying mistakes so that you can avoid them yourself.

Over-extending yourself financially

It is easy to get swept up in the excitement of buying a new home. One common home buying mistake is to make an offer on a house that will over-extend you financially. Even though you may qualify for the mortgage, it might put too much financial pressure on you. *You do not want your new home purchase to add stress to your life.* You should make sure that the monthly payment is something that you can comfortably afford.

Making significant financial changes prior to closing

Another common home buying mistake is to make some sort of financial change *before* closing. The approval for your mortgage is based on the financial information that you provided to the lender. Buying a new car, changing jobs, or even adding to your credit card debt can affect your ability to qualify for the loan that you need. *Avoid making any big purchases or job changes until after you close on your home.*

Not planning for resale

In today's mobile society, relatively few people stay in the same home for the full term of the mortgage. A common home buying mistake is to forget to buy with resale of the home in mind. Make sure that it is, for example, not too close to major roads or that it does not have an awkward floor plan. Buy a house that you are confident will be easy to sell when the time comes.

Not having a final walk-through

One of the last steps before closing is the final walk-through. Many buyers make the mistake of thinking that this is not necessary. It is important that all contingencies from the inspection have been taken care of and that you make sure that the home is in move-in condition. Make the time to have a final walk-through so you'll be sure the home is ready *prior* to closing.

Forgetting to take care of the little details

There is so much to do when buying a home. Don't make the common home buying mistake of forgetting to take care of all the details. Make a list of transferring all of the services at your current residence to your new residence and check them off as you make the change to avoid this common home buying mistake.

To ensure that you avoid these common home buying mistakes, consult with your Realtor. They are the experts and will make sure your home buying experience goes as smoothly as possible.



How Much Home Can You Afford?

If you're like many first-time or second-time homebuyers, chances are you've been spending your weekends driving around visiting open houses and new model homes. This is a great way to get a feel for what you want. The problem is that what you want isn't always what you should get, or what you can afford.

Before you start touring homes for sale, it's important to start off with a budget so you know how much you can afford to spend. Knowing what mortgage payment you can handle will also help you narrow the field so you don't waste precious time touring homes that are out of your reach.

Where to begin

The key factor in figuring how much home you can afford is your debt-to-income ratio. This is the figure lenders use to determine just how much mortgage debt you can handle, and thus the maximum loan amount you will be offered. The ratio is based on how much personal debt you are carrying in relation to how much you earn, and it's expressed as a percentage.

The ideal ratio

Mortgage lenders generally use a ratio of 36 percent as the guideline for how high your debt-to-income ratio should be. A ratio above 36 percent is seen as risky, and the lender will likely either deny the loan or charge a higher interest rate. Another good guideline is that no more than 28 percent of your gross monthly income goes to housing expenses.

Doing the math

First, figure out how much total debt you (and your spouse, if applicable) can carry with a 36 percent ratio. To do this, multiply your monthly gross income (your total income before taxes and other expenses such as health care) by .36. For example, if your gross income is \$6,500:

$$\begin{aligned} & \$6,500 \text{ (Gross monthly income)} \\ & \times .36 \text{ (Debt-to-income ratio)} \\ & = \$2,340 \text{ (Total allowable monthly debt payments)} \end{aligned}$$

Next, add up all your family's fixed monthly debt expenses, such as car payments, your minimum credit card payments, student loans and any other regular debt payments. (Include monthly child support, but not bills such as groceries or utilities.)

From the Inside: "A Home Equity Loan vs. a Home Equity Line of Credit...What's the Difference?"

If you're a homeowner, you can borrow against the value of your house through either a home equity line of credit (often called a HELOC) or a home equity loan (often called a HEL). Both are essentially a second mortgage.

What's the difference?

A HELOC allows you to draw funds, up to a predetermined limit, whenever you need money. There is generally a minimum payment due each month, with the option to pay off as much of the line as you want. The way that you draw and repay funds for a HELOC is similar to the way you draw and repay funds for other revolving lines of credit, such as a credit card. With a HEL, you receive a lump sum of money and have a fixed monthly payment that you pay off over a predetermined time period. In each case, the amount you can borrow is based on factors such as your income, debts, the value of your home, how much you still owe on your mortgage and your credit history.

The appeal of both of these types of loans is their interest rates, which are almost always lower than those of credit cards or conventional bank loans because they are secured against your home. In addition, the interest you pay on a home equity line or loan is often tax deductible (always consult your tax advisor about your particular situation).

Minimum monthly credit card payments*:

+ Monthly car loan payments:

+ Other monthly debt payments:

= Total monthly debt payments:

*Your minimum credit card payment is not your total balance every month. It is your required minimum payment — usually between two and three percent of the outstanding balance.

To continue with the above example, let's assume your total monthly debt payments come to \$750. You would then subtract \$750 from your total allowable monthly debt payments to calculate your maximum monthly mortgage payment:

$$\begin{aligned} & \$2,340 \text{ (Total allowable monthly debt payments)} \\ & - \$750 \text{ (Total monthly debt payments other than mortgage)} \\ & = \$1,590 \text{ (Maximum mortgage payment)} \end{aligned}$$

In this example, the most you could afford for a home would be \$1,590 per month. And keep in mind that this number includes private mortgage insurance, homeowner's insurance and property taxes.

Exceptions to the 36 percent rule

In regions with higher home prices, it may be hard to stay within the 36 percent guideline. There are lenders that allow a debt-to-income ratio as high as 45 percent. In addition, some mortgage programs, such as Federal Housing Authority mortgages and Veterans Administration mortgages, allow a ratio higher than 36 percent. But keep in mind that a higher ratio may increase your interest rate, so you may be better off in the long run with a less expensive home. It's also important to try to pay down as much debt as possible before you begin looking for a mortgage, as that can help lower your debt-to-income ratio.

To help you determine just how much home you can sensibly afford, feel free to contact our office today. We're here to help!

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Which is best for you?

Generally, a HELOC is a good choice to meet ongoing cash needs, such as college tuition payments or medical bills. A HEL is generally more suitable when you need money for a specific, one-time purpose, such as buying a car or for a major renovation.

Comparing the costs

Both HELOCs and HELs usually carry a slightly higher interest rate than that of a first mortgage. With a HEL, you may choose either an adjustable rate that fluctuates according to variations in the prime rate, or you may opt for a fixed rate. A fixed rate enables you to budget a set payment monthly without worrying about increasing costs should interest rates rise. With a HEL, there are also closing costs that you should consider.

A HELOC usually carries a slightly lower initial interest rate than a HEL, but its rate fluctuates according to the prime rate, so there is more interest rate risk.

For more information or to help you determine which type of loan is best for you, contact our office today!

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