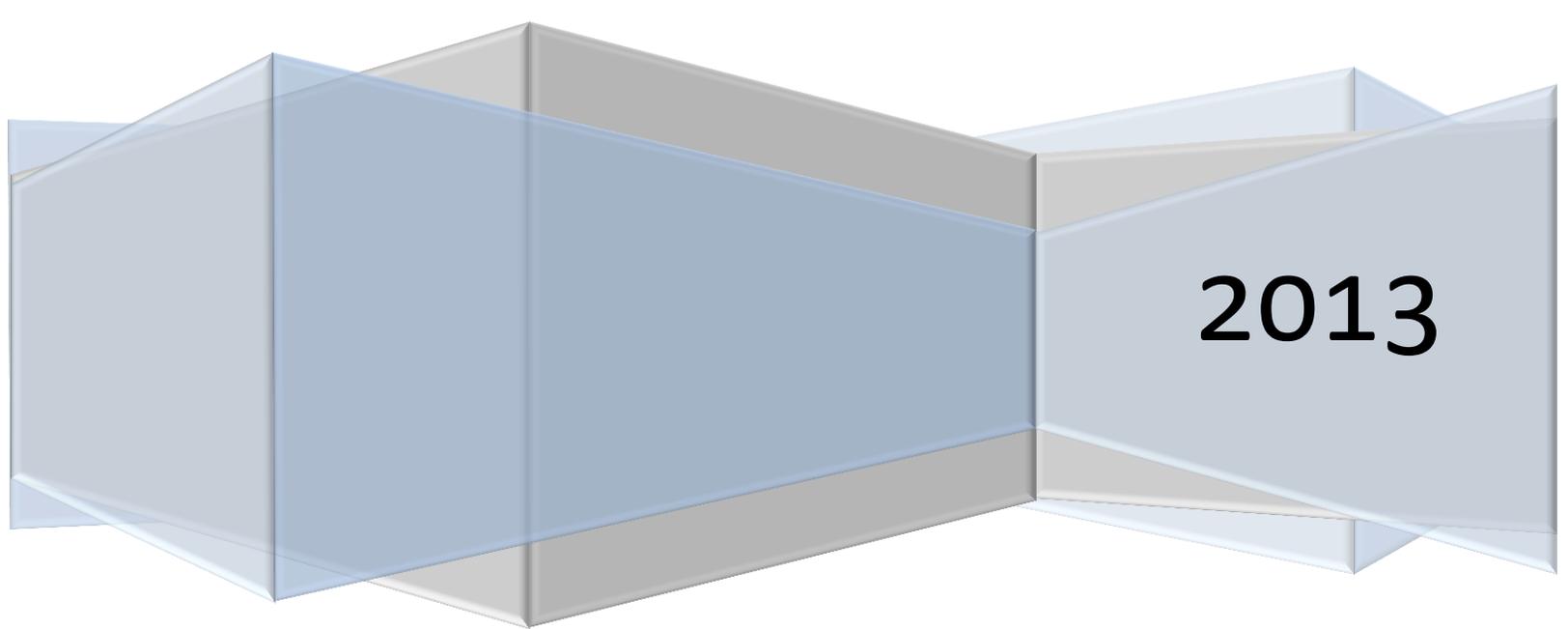




ROCKBRIDGE
INVESTMENT MANAGEMENT

Home Mortgage Search Process

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2013

Introduction

The purpose of document is to provide home mortgage shopping information for new home buyers and existing home buyers looking to refinance. It covers the different parts of the home loan search and process to help buyers achieve the best rate for their needs.

Types of Home Loans

- Conventional – This is currently the best loan type for most people. Conventional loans have a fixed interest rate and can vary in duration from 10 years to 30+ years. This is also the most difficult type of loan to qualify for, often requiring a 10% down payment and good credit.
- Federal Housing Administration (FHA) – A FHA loan is insured by the US Government and often has lower qualification criteria than a Conventional loan, however there are additional costs with a FHA loan that make them prohibitive for individuals with good credit and an available down payment.
- Adjustable Rate Mortgage (ARM) – An adjustable rate mortgage has a fixed interest rate for a number of years and then is variable annually based on a published benchmark such as the London Interbank Offered Rate (LIBOR).

Types of Lenders

- Mortgage Brokers – Mortgage brokers shop around for the best mortgage for given a buyer's circumstances. In return for their services, they are paid a slice of the mortgage value. Mortgage brokers can be very helpful for individuals with special circumstances such as poor credit, a low down payment or a high loan-to-income ratio.
- Direct Lenders – Direct lenders have the actual money to lend. The two types of direct lenders are:
 - Brick and Mortar – These direct lenders usually have a bank located in your town where you can visit and complete the entire mortgage process in person.
 - Internet – Internet lenders have a home office located in the US, but virtually all of their loans are completed through the internet/phone/mail. The loan rates are often better than Brick and Mortar lenders since overhead costs are lower.

Buying Criteria

- Attempt to have a 20% down payment to avoid Private Mortgage Insurance (PMI). If 20% is unrealistic, a 10% goal for a Conventional mortgage is usually reasonable. With FHA loans, the down payment can be as small as 3.5% of the loan value.
- Remember, the bigger the house, the more taxes and utilities you will pay along with the larger mortgage.
- Overall, a good option is to buy a home you will be happy with for many years in the future, but try and avoid approaching the buying criteria maximum limits.

What are Points?

- Points are pre-paid interest to the lender at closing in return for a lower interest rate of the course of the loan. One point is equal to 1% of the loan value, so if the loan is for \$200,000, then 1 point would be \$2,000 in pre-paid interest.
- There is a break even period for every loan interest rate/point combination. If the house is planned on being owned for an extended period of time, points are often worth purchasing.
- Each bank offers a different point vs. interest rate spread depending on their lending needs, requiring inquires at many different banks to obtain the best mortgage rate.

What is Private Mortgage Insurance (PMI)?

- Private Mortgage Insurance is required on all home loans with a loan-to-value ratio of greater than 80% (less than a 20% down payment on the home). The insurance protects the bank in case of a home mortgage default.
- PMI has to be paid on all three main types of loans.
- Conventional Loan PMI is based upon the down payment amount on the home. A 15% down payment will have a smaller PMI payment requirement compared to a 10% down payment.
- FHA loans have stipulations that require PMI to be paid for a certain period of time regardless of the loan-to-value ratio (5 years on a 30-year loan)

How Much Home Can I Afford?

- The first step is to look at what requirements you will want and need in a home. How many bedrooms/bathrooms? What school district? What neighborhood?
- Home purchase prices will vary depending on the location and personal preferences of the buyers, but there are 3 primary ways to determine the maximum home you can afford:
 - Maximum purchase price of 3x annual gross household income
 - Housing related payments (mortgage, taxes, homeowner insurance) should be less than 28% of your monthly gross household income
 - Total debt payments should be less than 36% of your monthly gross household income
- In order to be sure that you can afford the house you are looking at, lenders will “pre-qualify” applicants for a loan amount. This is a quick process (usually less than 15 minutes) and will help solidify the maximum mortgage a lender will provide.
- Determine how much you are willing to pay between the mortgage principal and interest, taxes and insurance. This value may be far less than the maximum a lender will provide.

How to Get the Best Mortgage for You?

- Determine the length of time you want to pay for the mortgage. 15 or 30-year mortgages are the two most common options.
- Determine how the duration you expect to live in the home. This will have an effect on the number of points paid.
- With today’s historically low interest rate environment, we recommend limiting the mortgage search to fixed rate mortgages.

Should I Refinance?

- A good rule of thumb is that it is worth refinancing if your interest rate is 1% higher than current market prevailing rates.
- For every individual situation, it is best to look at the simple math. If a refinance will cost \$4,000 and will save \$200/month, then the payback period is 20 months. With this calculation, make sure the timeline are similar. If there is 15 years left on a mortgage, compare rates when refinancing to a 15 year mortgage.
- Refinancing is a long process (3-6 months) and will involve quite a bit of paperwork. This is not a work free transaction and your time should be considered in the overall savings value.
- There are also additional considerations when refinancing.
 - How secure is your job?
 - How long do you plan on remaining in the house?
 - When would you like to have the house paid off?

Information Needed Before Mortgage Shopping

- Credit Rating or a good estimate of a Credit Score This can be found at <https://www.annualcreditreport.com/cra/index.jsp>
- Location of the property (City/State)
- Loan type and duration
- Home purchase or home refinance

Mortgage Rate Shopping Table

- To shop for different rates, call various banking institutions and tell them that you are looking for the available rate-point combinations for a 30-year conventional mortgage located in New York for 2 individuals that have a 750 credit score. (An example case). Without a long discussion, you should be able to find out the current rates to fill in the table below. (A few bank options are listed below, but it is not an all-inclusive list)

| Lender | 0 pts | 1 pt | 2 pts | 3 pts | Lender Fees |
|----------------------|-------|------|-------|-------|-------------|
| Local Credit Union 1 | | | | | |
| Local Bank 1 | | | | | |
| First Internet Bank | | | | | |
| Chase | | | | | |
| AmeriSave | | | | | |
| PenFed | | | | | |
| Bank of America | | | | | |
| Lending Tree | | | | | |
| Quicken Loans | | | | | |
| Citibank | | | | | |
| Wells Fargo | | | | | |

*Mortgage rates change daily, so this list will help you find the best option only when you are ready to purchase or refinance a home. A link to local bank rates in Syracuse, NY can be found here. <http://www.syracuse.com/mortgagerates/>

Selecting the Best Mortgage Option

- After obtaining a reasonable sample of mortgage options, most lenders will be out of the running. Determining the best interest rate-point combination must be weighed on the funds available for closing, the planned time spent in the house, payback period for each option, and willingness to work over the internet.

Closing Costs

- Most mortgages will have some form of closing costs associated with them. The fees cover the loan recording and processing, attorney costs, title insurance, appraisal and various other new mortgage requirements. Expect closing costs to be approximately 3%-5% of the loan value.
- Points and escrow (an account at the bank that accumulates taxes and insurance payments) are in addition to closing costs and will also need to be paid when opening a new mortgage

Closing Process/Timeline

- Once all of the paperwork is completed and the contract is signed, it can take between 30 to 90 days to close on a home and actually transfer ownership. This process can be even longer for foreclosures and short sales.

Summary

- Home ownership is one of the most rewarding aspects of life. Hopefully this document sheds some light on the complicated process and allows a smoother path to home ownership. If there are any questions regarding finances and investing, please feel free to contact Rockbridge.