

Real Estate Report:

HELP!!! Which type of loan is best for me?

By Thomas Lee

Before you are ready to make an offer on a home, you need to have your financing in order. Your agent will refer you to a lender who is usually part of her or his team. Your lender will help you get pre-qualified for your loan and will recommend the right type of loan based on your circumstances. Furthermore, your lender will make the entire loan process smooth by guiding you through the paperwork maze.

This information report was written to help you understand the basic differences between the types of available loans. This should help you determine the best type of loan for your circumstances. Talk to your real estate agent! She or he will explain any questions you have, including how the process works. Most importantly, your agent will refer you to a favorite lender who will pre-qualify you.

FHA Loans

FHA Loans are insured by the Federal Housing Authority and require a small down payment, typically in the 2.5 to 5 percent range. FHA loans are very popular with first time homebuyers who do not have a lot of cash to use as a down payment. Most FHA buyers are in the \$150,000 purchase range.

FHA loans have several advantages and disadvantages. They require a small down payment and usually allow for higher debt-income ratios (it's easier to qualify). Also, FHA loans are assumable (you can assume someone else's FHA loan and vice versa). However, you must pay dual insurance on FHA loans. Since FHA loans are considered higher risk, you have to first pay an up-front MIP (mortgage insurance premium) one-time fee in the case of loan default. Also, a second MIP is factored into your monthly payments. Finally, since FHA loans are considered a higher risk, the interest rates are usually higher than conventional loans.

VA Loans

VA Loans are guaranteed by the Veteran's Administration. You must be in the military, or a veteran, to qualify. The largest benefit of VA loans is you don't need a down payment, and very little cash to move in. On the downside, VA loans require a funding fee that is typically "rolled into" the loan. This means your mortgage can be substantially

higher than the value of your home. If you plan to live in the home for a short period of time, you run the risk of losing money when you sell. In this scenario your mortgage obligation could be higher than the market value of your home. Furthermore, VA lenders typically require very tough inspections, which can bog down the home buying process.

Conventional Loans

Conventional loans are the most popular type of loans.

Generally, the more you put down, the less of a risk you are to lenders. If you put down at least 20% of the purchase price of the loan, you won't have to pay PMI (private mortgage insurance that lenders require to protect themselves in case you default). Also, if you put down at least 20%, you are likely to get a lower interest rate. If you put down less than 20%, you will be required to pay the PMI, which will be built in to your monthly mortgage payments.

Conventional borrowers typically pay all of their own closing costs. Furthermore, the appraisal process focuses entirely on the market value of the home, not necessarily the condition it is in.

Fixed rate versus adjustable rate loans

When you choose your loan, you will have the option of getting a fixed or adjustable interest rate. The advantage of fixed-rate loans is the ability to lock in a low interest rate (if interest rates are currently low) for the lifetime of the loan. There's a lot of security knowing your payments will be the same year after year!

If interest rates are high, consider an adjustable rate mortgage (ARM). The interest rates on your loan adjust up and down, depending on the index the rate is tied to. With an ARM, if interest rates go up, your mortgage payments will go up (there IS a cap on how much they can go up each year). Conversely, if interest rates go down, so will your mortgage payments. The advantage of an ARM is interest rates are currently high, you can make mortgage payments based on current interest rates in hopes that eventually interest rates will fall. Once they fall, you can refinance your adjustable rate mortgage into a fixed mortgage and lock-in lower interest rates for the lifetime of the loan. On the downside, if interest rates continue to rise after you get an adjustable rate mortgage, the monthly payments can become onerous.

Term of the loan: 30 year vs. 15 year

Loans typically come in 10, 15, 20 or 30 year terms. By far, 30-year loans are most common. The advantage of a longer-term loan is the much lower mortgage payments spread out over 360 months. The downside is the higher amount of interest you will have to pay over the lifetime of the loan. Shorter term loans are will save you a lot of money interest. However, the monthly payments are much higher (typically 15 year mortgage payments are 25% higher than 30 year payments).

I hope this informational report was informative. As your local real estate professional, I am available to answer any questions you have about the best type of loan for your circumstances. You can call me at any time for advice, and please remember that you are under no obligation or pressure of any kind. I would very much like to help you.

Best Regards,

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