



What's Your Home Buying Power?

If you're in the market for a new home or investment property, one of the first questions you'll probably ask is, "What can we afford?" Many buyers become so caught up in how much they can afford that they don't realize their total buying power—that is, the total amount of purchasing potential they actually have.

BUYING POWER DEFINED

Your buying power is comprised of the total amount of money you have available each month for a mortgage payment. This means the money you have each month after fixed bills and expenses. Any money you've saved for a down payment, the proceeds from the sale of your current home, if applicable, and the amount of money you're qualified to borrow all impact your buying power as well. When you take all of this into account, you may find you are able to purchase a larger home or a home in a more desirable neighborhood, or you might realize you should be looking for homes in a lower price range.

WHY BUYING POWER MATTERS

A common misunderstanding is that a home's list price determines whether or not you can purchase it. Although it's important to look at the price tag, it's essential to consider what your monthly payment will be if you own the home. After all, the purchase price doesn't include the housing-related expenses, such as annual property taxes, homeowner insurance, associated monthly fees and any maintenance or repairs. Figuring out the payment will prevent you from overestimating or underestimating your buying power. Remember, you'll live with your monthly payment, not the sales price.

Once you have clarity on your buying power, you'll be able to buy the home you want, instead of settling for a home because you feel it's the only one you can afford. It will also prevent you from becoming "house poor," a common term for someone who's put all their money toward the down payment, leaving them nothing left over for fees outside of their monthly house payment. Both scenarios can negatively impact the lifestyle you want to live. Understanding your buying power can help you get the home you want without sacrificing the lifestyle you desire.

CALCULATING YOUR BUYING POWER

You might be wondering, "How do I know what my buying power is?" Buying power is calculated by adding the money you've saved for a down payment and/or the money you made from selling your home (minus fees and mortgage payoff) to all of your sources of income and investments that could be used to make your monthly payment. Make sure to include your monthly pay, commissions or tips, dividends from investments, payments from rental properties or other monthly income you receive as well as the loan amount you're willing to finance and can qualify for.

Most lenders advise buyers to spend no more than 35 to 45 percent of their pretax income on housing, meaning all your income and sources of revenue prior to paying taxes. Make sure you factor in not only your mortgage payment, but also property tax and home insurance to the cost of housing.¹ However, other financial experts advise spending no more than a very conservative 25 percent of your after-tax income. Whether you plan to spend the average, play it conservative or split the difference is up to you. While it's tempting to take out a large loan in order to purchase the home of your dreams, keep in mind the less money you have to borrow, the stronger your buying power may be.

Mortgage lenders say the ideal housing expense ratio should be a ratio of 28% or less.²

DON'T FORGET TO FACTOR IN PROPERTY TAXES AND INSURANCE

These are often added to your principal and interest of your mortgage payment—the money used to pay down the balance of your loan and the charge for borrowing the money. Since these numbers vary, contact your county assessor's office for the current property tax rate and your insurer for a home insurance quote. Once you have these figures, divide each by 12 to estimate how much they'll add to your payment amounts.

FIGURE OUT YOUR BUYING POTENTIAL

What's your buying potential? Fill out this worksheet to get an estimate.

Housing Expense Ratio:		
1.	Monthly income before taxes.	\$
2.	Multiply line 1 by 0.28	x 0.28
3.	Monthly mortgage payment (PITI) should not exceed this amount	= \$
4.	Monthly income before taxes	\$
5.	Multiply line 4 by 0.36	x 0.36
6.	Total monthly payments on all debts (including mortgage) should not exceed this amount	= \$
7.	Subtract the total monthly payments on all outstanding debts (e.g., car loans, credit cards, student loans, etc.)	-\$
8.	The monthly mortgage payment should not exceed this amount	\$
9.	Look at line 3 and line 8. The lower figure is an estimate of the maximum mortgage payment in consideration of your income and debts.	\$
10.	Multiply line 9 by 0.80	x 0.80
11.	This equals portion of your mortgage payment that is the principal and interest only	\$
12.	Use the table below to see the size of the loan you may be able to obtain with this monthly mortgage payment.	

Source: Iowa State University Extension, What is your house-buying power?

Monthly Payment on 30-Year Fixed Rate Mortgage ⁴							
Loan amount	3%	3.5%	4%	4.5%	5%	5.5%	6%
\$50,000	211	225	239	253	268	284	300
\$75,000	316	337	358	380	402	426	450
\$100,000	421	449	477	506	536	568	600
\$150,000	632	674	716	759	804	852	900
\$200,000	842	898	954	1012	1072	1136	1200
\$250,000	1052	1123	1193	1265	1340	1420	1500
\$300,000	1263	1347	1431	1518	1608	1704	1800

Sources: 1. Moneyunder30.com

2. Credit.com

3. Iowa State University Extension, What is your house-buying power?

4. HSH.com

If you haven't sold your current home yet, a Comparative Market Assessment (CMA) will give you a general idea of how much you may get for your home based on what other homes have sold for in your area. Contact our team for a FREE CMA!

Do you want a clearer picture of your buying power? Would you like to see what kind of homes you can get with your buying power? Give us a call!

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