

INDIVIDUAL BORROWING LESSON:

HOW MUCH HOUSE CAN YOU AFFORD?: STUDENT HANDOUT

Congratulations! You were able to save and invest more than 10 percent of your budget over a few years, and you now have \$10,000 for a down payment on a house. Better yet, you have a good credit score of 700. You are going to need a mortgage. Start by checking out the current rates. Go to the following Web site: <http://realestate.yahoo.com/loans/>.

Scroll down to the box that lists "Mortgage Rate Trends and Averages."

Click "Change Location," and enter your ZIP code to see local rates.

1. What is the typical rate for a 30-year fixed-rate mortgage?
2. What is the rate for a 5/1-year adjustable-rate mortgage (ARM)?

Note: A fixed-rate mortgage has an interest rate that never changes over the term of the loan, while an ARM, or adjustable-rate mortgage, can go up or down. 5/1 means the rate is fixed for five years and can't go up by more than 1 percent a year thereafter. This type of rate is good if you absolutely know you will live in the house for only three to five years.

Congratulations again! You graduated high school. According to the U.S. Census Bureau, the average high school graduate earns approximately \$30,000 a year. Better yet, you went on to college and earned a bachelor's degree and along with it an income of \$52,000 a year. You even went on to get your master's degree, and you now earn \$62,000. You budget well and have no credit card debt. Now see what house price will be affordable with

each of the different salaries. A general guideline is that you should not spend more than one-third of your budget on debt payments.

Click the link at the top of the page for "Calculators." Now click the link titled "How Much House Can I Afford?" Enter the following information:

- ∞ Your income (\$30,000 first for the high school graduate)
- ∞ \$150 car payment
- ∞ No credit card debt or other payments
- ∞ Your local interest rate for a 30-year fixed-rate loan
- ∞ 30 (years) for term of new mortgage
- ∞ \$10,000 for down payment
- ∞ \$2,000 in property taxes
- ∞ \$500 for insurance

Click "Submit."

How much house can you afford if you earn the average high school graduate's salary?

Repeat the steps to determine how much house you can afford on the other two salaries.

How much house can you afford if you earn the average college graduate's salary?

How much house can you afford if you earn the average master's degree graduate's salary?

One question you might ask is does it make sense to buy a house, or is it better and easier to rent? Click the link at the top of the page for "Calculators." Now click the link titled "Should I Rent or Buy a Home?" According the U.S. Census, the average American rental housing cost is \$650 per month. (Rent is much higher for new buildings and for higher-valued regions.) Enter the following information:

- ∞ A \$650 month rent payment
- ∞ 4 percent annual rent increase
- ∞ The home price a college graduate can afford (from above)
- ∞ 5 percent annual home price appreciation rate
- ∞ An amount of a loan that is 90 percent of your house price (the other 10 percent was your down payment)
- ∞ The interest rate for a 30-year loan (from above)
- ∞ \$500 in homeowner's insurance
- ∞ \$2,000 annually in property taxes
- ∞ \$1,000 in maintenance costs (remember when you rent, the landlord takes care of the maintenance)

∞ Change the number of years for comparison to five

Click submit.

Under this scenario, would you be better off buying or renting, and by how much? (The answer is at the top of the page.)

Click the link at the top of the page titled "Find a Home. " Enter your ZIP code, and next to "price," change the price to the highest amount affordable for someone with a master's degree. Click "search." You can keep searching by clicking the search button again on the next page. You can sort in a variety of ways, including from low price to high and by the number of bedrooms available. Try to find a house you like that fits your future master's degree budget. If you can't find a house you like in your area, keep searching by scrolling down and choosing a different city or homes within 50 miles. Describe a house that was for sale that you liked and that fit into your budget.

Now all you need to do is get a preapproved loan offer from a mortgage lender and perhaps a real estate agent to help you through the process. You are on your way to taking the right steps to own a home that fits within your budget.

