



Can They Afford to Buy?

For each case study, examine the household's overall financial portfolio and determine whether they are able to realistically afford the home they would like. Your decision should be based on three key lending criteria – (1) ratio of monthly debt payments to income, (2) ratio of monthly housing expenses to income, and (3) ability to make a down payment. Use the following questions as a guide to assess each household's financial situation.

1. Are the household's total monthly debt payments \leq **36%** of their gross monthly income (*back-end ratio*)?
2. Are the household's total monthly housing expenses \leq **28%** of their gross monthly income (*front-end ratio*)?
3. Is the household able to make a down payment \geq **20%** of the home's purchase price?
4. Based on these three criteria, would you "approve" or "deny" their loan request? Why or why not? If you would "deny" their request, do they need to have more realistic expectations about how much home they can afford? What can the household do to improve their financial situation?



CASE STUDY 1: Meet the Chen Family

David and Maria Chen just had their first baby, Jacob, a year ago. David is currently making \$84,000 as a computer programmer for a major technology company. Since having the baby, Maria has been working at home taking care of Jacob. Right now, the Chens are living in a 1-bedroom apartment. Their monthly rent is \$750. With the new baby, space is getting tight and they would like to purchase their first home. They have been saving up and have set aside \$34,000 for a down payment. The house they are interested in purchasing is valued at \$174,000. A 30-year fixed mortgage at 6.5% interest would put their monthly mortgage payment at \$1,226. Given their current financial situation, can they afford to move out of their apartment and purchase this home?

Summary of Financial Portfolio

Monthly Income

Gross annual income	\$84,000
Gross monthly income (\$90,000 / 12 months)	\$7,000

Monthly Debt Payments

Mortgage payment	\$1,226
Car payments	\$350
Credit card payment(s)	\$250
Student loan payment(s)	\$350
Installment loan payment(s)	\$0
Other monthly loan payments	\$0
<i>Total monthly debt payments</i>	<i>\$2,176</i>

Monthly Housing Expenses

Mortgage payment (principal and interest)	\$914
Property taxes	\$218
Mortgage and hazard insurance	\$94
<i>Total monthly housing expenses</i>	<i>\$1,226</i>

Total Assets

Checking and savings accounts	\$45,000
Investments (e.g., CDs, bonds, mutual funds, stocks)	\$74,000
Property (e.g., real estate, cars)	\$15,000
Retirement accounts (e.g., IRA, pension)	\$112,000
<i>Total assets</i>	<i>\$189,000</i>

Total Liabilities

Mortgage debt	\$144,500
Car loans	\$5,000
Credit card debt	\$2,500
Student loans	\$14,000
Installment loans	\$0
Home improvement loans	\$0
Other debt	\$0
<i>Total liabilities</i>	<i>\$166,000</i>



CASE STUDY 2: Meet Chantelle

Chantelle has been working as a hospital administrator for the last ten years. She's been actively contributing to her retirement account at work and has been slowly saving up to buy her first home. She found a great fixer-upper for a fabulous price. She fell in love with the house the moment she saw it and "it's a must have." Currently, she lives with a roommate in a 2-bedroom apartment. Her share of the monthly rent is \$525. At this time, Chantelle is able to make a down payment of \$24,000. The house she is interested in purchasing is valued at \$78,000. The monthly payment for a 30-year fixed mortgage at 6.5% interest would be about \$623. Given her current financial situation, can she afford to purchase this fixer-upper?

Summary of Financial Portfolio

Monthly Income

Gross annual income	\$64,800
Gross monthly income (\$90,000 / 12 months)	\$5,400

Monthly Debt Payments

Mortgage payment	\$623
Car payments	\$360
Credit card payment(s)	\$350
Student loan payment(s)	\$400
Installment loan payment(s)	\$0
<u>Other monthly loan payments</u>	<u>\$0</u>
<i>Total monthly debt payments</i>	<i>\$1,733</i>

Monthly Housing Expenses

Mortgage payment (principal and interest)	\$464
Property taxes	\$111
<u>Mortgage insurance</u>	<u>\$48</u>
<i>Total monthly housing expenses</i>	<i>\$623</i>

Total Assets

Checking and savings accounts	\$18,000
Investments (e.g., CDs, bonds, mutual funds, stocks)	\$24,000
Property (e.g., real estate, cars)	\$8,000
<u>Retirement accounts (e.g., IRA, pension)</u>	<u>\$68,000</u>
<i>Total assets</i>	<i>\$52,000</i>

Total Liabilities

Mortgage debt	\$73,300
Car loans	\$10,000
Credit card debt	\$3,000
Student loans	\$18,000
Installment loans	\$0
Home improvement loans	\$0
<u>Other debt</u>	<u>\$0</u>
<i>Total liabilities</i>	<i>\$104,300</i>



CASE STUDY 3: Meet the Newlyweds

Erik and Susan just graduated from college. They also just got married and have started new jobs. Both are teachers working at the local high school. Erik is making \$35,000 and Susan is making \$37,000. They are currently living in a 2-bedroom apartment. Their monthly rent is \$625. They've been saving every penny they can to buy a condo. Recently, they went house hunting. They found a place they are very interested in purchasing, but are concerned it may be a little out of their price range. Right now, they are able to make a down payment of \$15,000. The condo they are interested in purchasing is valued at \$140,000. A 30-year fixed mortgage at 6.5% interest would put their monthly mortgage payment at \$1,072. Given their current financial situation, can they afford to purchase this new home?

Summary of Financial Portfolio

Monthly Income

Gross annual income	\$72,000
Gross monthly income (\$90,000 / 12 months)	\$6,000

Monthly Debt Payments

Mortgage payment	\$1,072
Car payments	\$350
Credit card payment(s)	\$400
Student loan payment(s)	\$450
Installment loan payment(s)	\$0
<u>Other monthly loan payments</u>	<u>\$0</u>
<i>Total monthly debt payments</i>	<i>\$2,272</i>

Monthly Housing Expenses

Mortgage payment (principal and interest)	\$816
Property taxes	\$175
<u>Mortgage insurance</u>	<u>\$81</u>
<i>Total monthly housing expenses</i>	<i>\$1,072</i>

Total Assets

Checking and savings accounts	\$19,000
Investments (e.g., CDs, bonds, mutual funds, stocks)	\$23,000
Property (e.g., real estate, cars)	\$15,000
<u>Retirement accounts (e.g., IRA, pension)</u>	<u>\$0</u>
<i>Total assets</i>	<i>\$57,000</i>

Total Liabilities

Mortgage debt	\$129,000
Car loans	\$18,000
Credit card debt	\$3,000
Student loans	\$34,000
Installment loans	\$0
Home improvement loans	\$0
<u>Other debt</u>	<u>\$0</u>
<i>Total liabilities</i>	<i>\$184,000</i>

CASE STUDY 4: Meet the Beckers



John and Sandy Becker have two children, Josh and Emily. They are currently living in a 3-bedroom home but would like to move into a larger residence. John and Sandy are working in executive positions, pulling in a combined income of \$180,000. While they have been actively saving and investing, they've also been trying to “keep up with the Jones,” spending and incurring a significant amount of credit card debt. Assuming they sell their current house for the expected asking price of \$285,000, they would be able to make a down payment on a new home of \$200,000 and use the rest to pay off some of their other debts. The house they are interested in purchasing is valued at \$420,000. A 30-year fixed mortgage at 6.5% interest would put their monthly mortgage payment at \$2,220. Given their current financial situation, can they afford to upgrade to a larger home?

Summary of Financial Portfolio

Monthly Income

Gross annual income	\$180,000
Gross monthly income (\$90,000 / 12 months)	\$15,000

Monthly Debt Payments

Mortgage payment	\$2,220
Car payments	\$450
Credit card payment(s)	\$4,000
Student loan payment(s)	\$600
Installment loan payment(s)	\$0
Other monthly loan payments	\$0
<i>Total monthly debt payments</i>	<i>\$7,270</i>

Monthly Housing Expenses

Mortgage payment (principal and interest)	\$1,458
Property taxes	\$526
Mortgage insurance	\$236
<i>Total monthly housing expenses</i>	<i>\$2,220</i>

Total Assets

Checking and savings accounts	\$26,000
Investments (e.g., CDs, bonds, mutual funds, stocks)	\$54,000
Property (e.g., real estate, cars, excludes current home)	\$42,000
Retirement accounts (e.g., IRA, pension)	\$560,000
<i>Total assets</i>	<i>\$682,000</i>

Total Liabilities

Mortgage debt	\$230,500
Car loans	\$23,000
Credit card debt	\$36,000
Student loans	\$32,000
Installment loans	\$0
Home improvement loans	\$22,000
Other debt	\$0
<i>Total liabilities</i>	<i>\$343,500</i>



DENIED