Buy A Home With A Low Down Payment

By Cathy King

Many people mistakenly believe you can't buy a house unless you have a down payment that equals 20 percent of the purchase price. The truth is many people buy homes every day with down payments of only three to five percent. They were able to do so thanks to government and community sponsored programs that make home ownership feasible for low income and first time buyers. Some communities work with Fannie Mae (the federal government's home ownership assistance corporation) to provide flexible mortgage options for police officers, firefighters, teachers and healthcare workers. These programs are structured to offer lower down payments as well as reduced income requirements to qualify.

Fannie Mae loans are designed for people with modest incomes who want to become homeowners. Typically, a three percent down payment is required for a 25 or 30 year fixed mortgage and the borrowers must attend a homebuyer education seminar in order to qualify.

The Federal Housing Administration has a program called FHA that insures residential loans made by private lenders. If you qualify for an FHA loan, you can purchase a home with a down payment of three to five percent of the FHA appraised value or the sale price, whichever is lower. FHA mortgages have a maximum loan limit determined by average home prices in a particular region.

Veterans applying for a home loan through the Veterans Administration may buy a home up to specified limits with no down payment. Generally it is easier to qualify for a VA loan than an FHA or conventional home loan. Your local VA office can help you determine if you are eligible and discuss the loan limits and other procedures with you.

The Rural Housing Service, an agency of the Department of Agriculture, offers low interest and no down payment loans to farmers and others who want to purchase property in rural areas and who have been denied loans from other lenders. Your local RHS office can let you know if you qualify and help you with the application process.

Requirements for low down payment loans differ slightly, but most require that you have enough income to support a monthly mortgage payment and the cash available to cover the down payment. You will also need to cover the cost of closing and other fees that may be necessary such as appraisals. A good credit history is important and you may need to prove you have enough money in savings to make at least two monthly mortgage payments. You will also need to buy homeowner's insurance sufficient to meet the requirements of the lender. Mortgage insurance is almost always required in low down payment purchases to protect the lender from loss if the homeowner can't make the monthly mortgage payments.

In approving a home loan lenders look for a borrower's ability to pay, which is determined by employment, and willingness to pay, which is based on how you have handled prior financial commitments. It is important to remember that lenders handle cases on an individual basis. You may be weak in one area and strong enough in another to tip the balance in your favor.

A qualifying ratio is used to determine how much mortgage a person can afford. Basically the ratio calculates the amount of money you have available to spend on mortgage payments based on your income and other financial obligations. For FHA loans the ratio is 29% of your gross monthly income. Conventional loans usually calculate the ratio at 26 to 28 percent of your gross monthly income. If your annual income is $40,000, your gross monthly income is $3076. (3076 x 28% = 861) Therefore, you should be able to afford a monthly payment of $861.

The lender will also take into consideration any other long-term debt that you owe such as car payments, outstanding student loans and credit card debt. When you are buying a home it is important to anticipate additional spending for maintenance, appliances, insurance and utilities.

An alternative homebuyers often overlook is seller financing. Some sellers who don't need all of the cash from the sale upfront may be willing to offer you a second mortgage or assist you with financing by offering a lease to buy option. If you decide to go with a seller financing arrangement, have the house thoroughly inspected for major defects and make sure the interest rate being offered is as low as what you could obtain through a mortgage lender.