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Mortgage Programs: Conventional vs. Non-Conventional Mortgages

Selecting a mortgage program starts with understanding the options. Conventional and non-conventional mortgages offer their own version of fixed rate mortgages, ARMs and reverse mortgages.

Learning Objectives:

- Describe the difference between conventional and non-conventional mortgages.
- Explain the criteria lenders and government sponsored enterprises use for loan qualification

This content is intended for informational purposes only. It should not be considered a substitute for advice from a professional.

Click on the first lesson below—or the “Start Course” button above—when you’re ready to begin.

 **What Are Conventional Mortgages? Pros and Cons**

 **What Are Non-Conventional Mortgages? Pros and Cons**

 **Summary: A Side-by-Side Comparison**

The 4 C's of Mortgage Qualification

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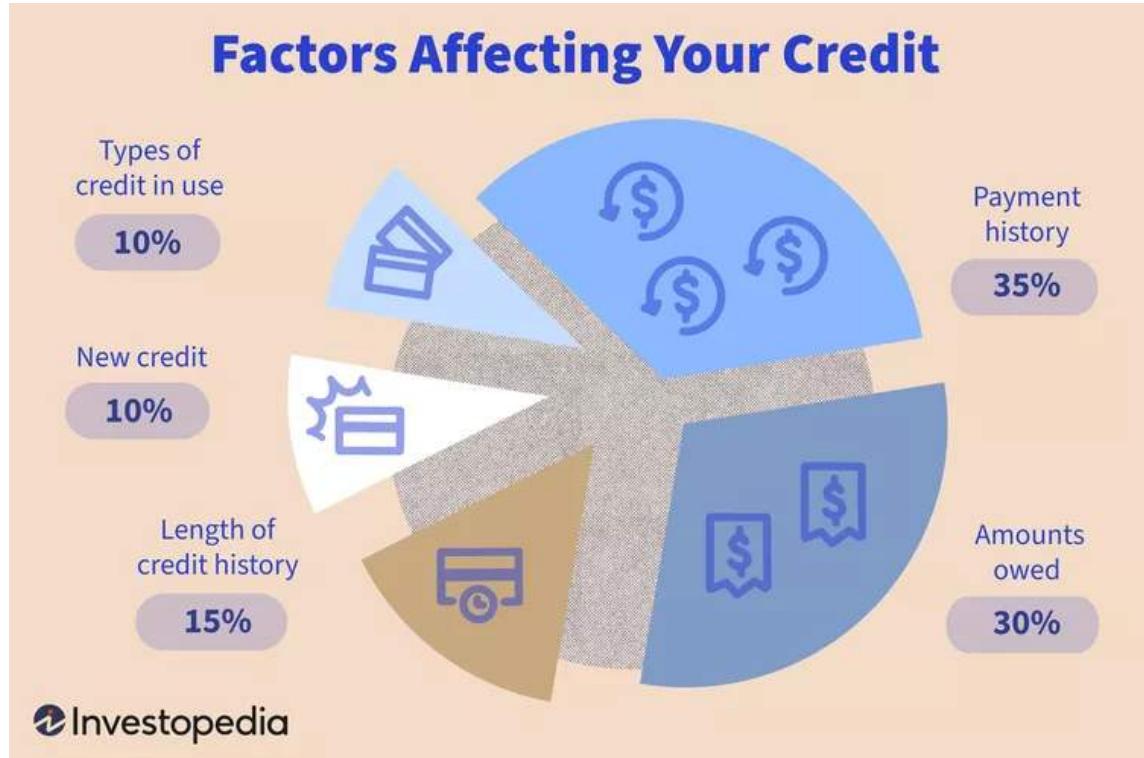
Review These Loan Qualification Requirements

To compare programs effectively, it is important to understand the loan qualifications government sponsored enterprises (GSE) and lenders use. Expand each term below to reveal its definition. Or, skip to the next lesson if you're already comfortable with the requirements.

CREDIT	CAPACITY	COLLATERAL	CASH
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Credit refers to the borrower's credit report, which includes their credit score and current debt obligations. Credit reports are a great indicator of how reliable borrowers have been at paying back debts.

For more information: [Review Credit](#).

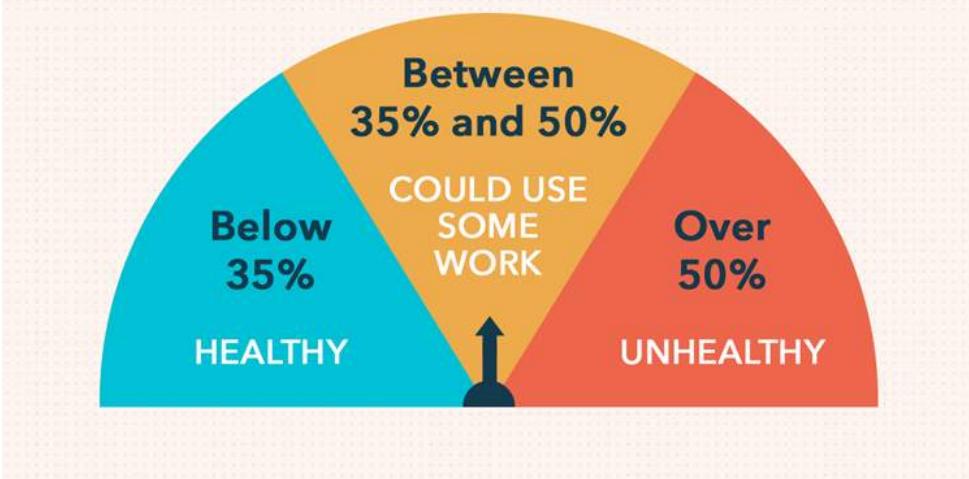


CREDIT	CAPACITY	COLLATERAL	CASH
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Capacity is the borrower's gross monthly income in comparison to their monthly debt (debt-to-income). This determines the loan amount affordable for the borrower.

For more information: [Review Mortgage Math](#).

Debt-to-Income Ratio Ranges



CREDIT

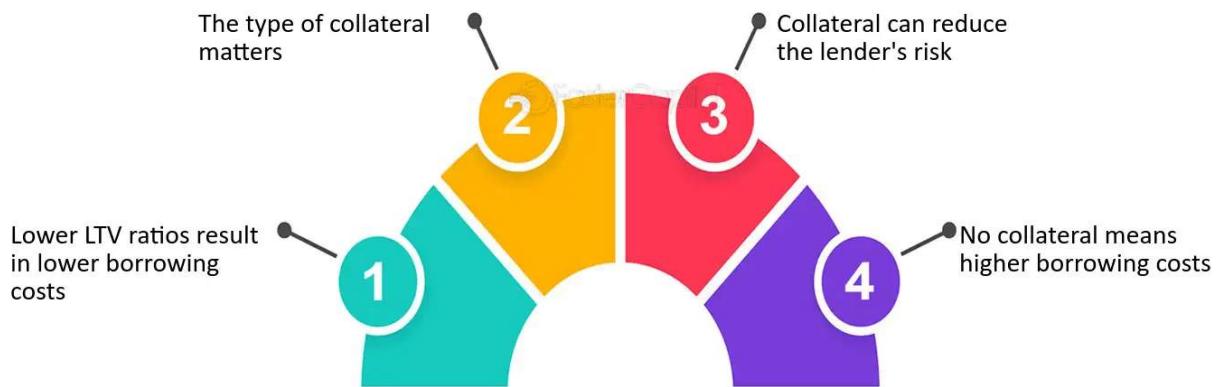
CAPACITY

COLLATERAL

CASH

Collateral is the loan amount compared to the value of the home (loan-to-value).

The Role of Collateral in Borrowing Costs



CREDIT	CAPACITY	COLLATERAL	CASH

Cash, also known as assets, is any money the borrower has in a bank account, retirement account, etc.

ASSET CLASSES

Diversifying your portfolio by investing in different types of assets can help protect you from volatility.



Cash

- Cash equivalents
- Money market funds
- U.S. Treasury bills
- Certificates of deposit (CDs)



Equities

- Stocks
- Dividend payments



Fixed Income

- Bonds



Alternative Investments

- Real estate
- Gold
- Silver
- Cryptocurrency
- Peer-to-peer loans

The Motley Fool 

Once you're comfortable with this vocabulary, continue to the following lessons to compare mortgage programs.

We'll introduce conventional first. Then, we'll move on to non-conventional. Finally, we'll provide a side- by-side comparison table in the course summary.

I'M READY

What Are Conventional Mortgages? Pros and Cons

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Conventional Mortgages

Conventional Mortgages are private programs neither backed nor insured by the government. However, they are usually the first place to start before exploring other options. Let's explore the pros and cons of conventional financing.

Distinguishing Program Feature	Pro or Con?
Wide array of options	<p>Pro: Lenders have more freedom to offer flexible options such as fixed versus variable-rate financing, and borrowers can typically avoid the extra cost of mortgage insurance if they put down a large enough amount (usually 20%).</p>
Higher loan limits	<p>Pro: The lack of government involvement means borrowers will usually be able to access more funds with a conventional loan. The limit on an FHA loan, one type of government-backed loan, currently sits at \$1.2 million for high-cost areas.</p> <p>For a conventional loan, on the other hand, borrowers may be able to borrow up to \$2 million if their credit score is high enough.</p>
Flexible interest rates	<p>Pro: Conventional loans can offer more flexible interest rates, especially for borrowers with a strong credit history. These loans also carry fewer extra costs, such as mortgage insurance or loan origination fees.</p> <p>Con: Although conventional loans can come with lower rates, this is generally only true for borrowers with high credit scores. A lower credit</p>

Distinguishing Program Feature	Pro or Con?
	score means more risk for the lender. Because of that, they'll charge more to cover the risk, especially since a conventional loan doesn't have a government agency as a safety net.
Requires a higher credit score	Con: A government-backed loan may be the only immediate option for borrowers with a low credit score. Fannie Mae's minimum qualifying score for a fixed-rate conventional loan is 620. Anything less is considered too risky for most lenders, so they'll want that added security of a government agency to offset their risk.



Remember to weigh the above pros and cons within the context of each customer's needs.

Why Choose a Conventional Mortgage?

Conventional loans have many advantages. For buyers with lower scores or less cash to bring to the table, though, it's worth exploring government-backed loan options. Conventional mortgages are generally best suited for people with the following:



You have a stable full-time job that provides regular, consistent paystubs.



You have a credit score of 650 or higher.



Your debt-to-income ratio is 35% or lower.



You can afford a 10–20% down payment for your loan.

CONTINUE

Using the information provided, select ALL of the buyers best suited for a conventional mortgage.



Gretchen has been working for a cable company for 20 years. Her credit score is 700, and her debt-to-income ratio is 10%.



Mike is a retired veteran, with a credit score of 600. He works as a general contractor 6 months out of the year, and has a debt-to-income ratio of 5%.



Fariyal has consistently worked for the last 7 years at a law firm. She can afford a 15% down payment, and her credit score is 750.



Dan has been a seasonal employee for 6 years with a landscaping company. He has minimal savings, and a credit score of 650. Due to inconsistent work, his debt-to-income ratio is 55%.

SUBMIT

Continue to the next lesson to learn about non-conventional mortgages.

CONTINUE

What Are Non-Conventional Mortgages? Pros and Cons

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Non-Conventional Mortgages

Non-Conventional Mortgages, also known as government mortgages, are backed and insured by the government. They were created to help individuals with low to moderate incomes and credit scores. Let's explore the pros and cons of non-conventional financing.

Distinguishing Program Feature	Pro or Con?
Lower credit requirement and down payment	Pro: Depending on the loan type, down payments can be as low as 0%. Additionally, non-conventional loans typically accept credit scores under 600.
Flexible payment options	Pro: Most non-conventional mortgages offer the opportunity to make lower monthly payments – or even pay off the entire principal balance in one lump-sum.
Restricted client pool	Con: Individuals who need help getting a home can pursue non-conventional mortgages. Therefore,

Distinguishing Program Feature	Pro or Con?
	loans are limited to certain groups, such as Native American or veteran buyers, or to rural properties.
Potentially high interest rates	<p>Con: Many non-conventional loans are adjustable-rate mortgages (ARMs) and have the potential to increase the rate at any time. Furthermore, rates may be higher to account for the risk of defaulting on the loan.</p>



Remember to evaluate the above pros and cons within the context of each customer's needs.

Why Choose a Non-Conventional Mortgage?

Non-conventional mortgages offer lower monthly payments and flexible payment options, often with less strict requirements than conventional loans. However, these flexible options can be dangerous to borrowers, especially when paired with higher rates. Non-conventional mortgages are best suited for people with the following:



You are self-employed or have unsteady employment history.



You are a veteran.



You have a credit score of 620 or lower.



Your debt-to-income ratio is more than 35%.



You require a lower down payment.

Using the information provided, select ALL of the buyers best suited for a non-conventional mortgage.



Toni has worked for a cable company for 18 years. Her credit score is 720, and her debt-to-income ratio is 10%.



Brandon is a retired veteran, with a credit score of 650. He works as a general contractor 6 months out the year, and has a debt-to-income ratio of 5%.



Dan has been a seasonal employee for 6 years with a landscaping company. He has minimal savings, and a credit score of 650. Due to inconsistent work, he relies on his credit cards and his debt-to-income ratio is 55%.



Arielle runs a catering business, and has a credit score of 615. Most of her income goes to paying down her credit card debt. She has a debt-to-income ratio of 60%, and has minimal savings.

SUBMIT

Now that you've learned about both conventional and non-conventional mortgages, continue to review a side-by-side comparison.

CONTINUE

Summary: A Side-by-Side Comparison

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Key Takeaways

You've learned the differences between the two main types of mortgage plans: **conventional** and **non-conventional**.

A Side-by-Side Comparison

The following table summarizes the main differences between conventional and non-conventional mortgage plans.

Conventional Mortgage	Non-Conventional Mortgage
Wide array of options	Lower credit requirement
Higher loan limits	Lower down payment
Lower out-of-pocket maximum	Flexible payment options
Flexible interest rates	Potentially high interest rates

Conventional Mortgage	Non-Conventional Mortgage
Requires a higher credit score	Restricted client pool
Best suited for individuals with a high credit score, low debt-to-income ratio, and a stable, long-term career.	Best suited for individuals with unconventional employment, lower credit score, high debt-to-income ratio, and veterans.



These points are generalities. Always evaluate the specific details of your loan options. Remember to weigh this information against your financial situation and family needs.

Thank you for completing this course!