How To Play The Mortgage Game, And Win!

By Tony Ferlazzo & Fran Ferlazzo

Homeownership!

We instinctively seek it, like a bird wants to build a nest. Yet without the money to pay for it, we have as much of a chance of owning our own home as a monkey has in joining the Army.

Few of us truly own their home free and clear. Most people use someone else's money to make homeownership a reality.

Obtaining a mortgage can be a stressful as filing tax returns, but it doesn't have to be that way. You should look at the process like you would if you were playing a game. There are rules and strategies for winning. If you want to play to win you need to understand these rules and strategies for winning. This special report will help you understand the rules so you can play the game better. Have less stress, and win at the mortgage game!

Two Games in One

Have you ever gone to the store to buy a chess game? Most people come home with a set of checkers along with their new chess set and board. The reason is that both chess and checkers are played on the same board even though they have a different set of rules and objectives.

It's the same way with obtaining a mortgage loan. There are two closely related games that are being played, one right after the other. The first one is called *Find The Money*. The second one is called *Profits Over Time*.

This eBook focuses on *Find The Money*. Look for another one of our eBooks, *Profits Over Time*.

Find The Money

The game has the same two players. You're familiar with both of them. The first is called the borrower and the second is called the lender.

A quick overview of *Find The Money*, the loan process:

Complete an application: After you have completed your application, it will be reviewed for completeness and accuracy.

Credit check: Using the information you provide, we will request the three major Credit Bureaus to provide us with a copy of your credit report.

Lender: Next, one or more lenders are located that will fit your specific needs. As a mortgage broker, we have over 120 lending institutions to draw from.

Proposal: Once a pre-qualification is received from the lender, a proposal is developed and a time for the presentation of that proposal is set with you.

Title and Escrow: After you approve the proposal, sign all disclosures, and give needed information (i.e. income documentation, hazard insurance binder, mortgage statements, credit card statements) to us, title and escrow is opened.

Inspections and appraisals: These items are required to insure and protect your investment in the home.

Signing: After the loan documents are received and evaluated, closing documents are produced and a signing appointment is made with you.

Funding conditions: After the documents have been signed and notarized, they are transported to the lender who then verifies the completeness and double checks the signatures and dates. The new Deed Of Trust is recorded with the county. Final conditions need to be met for funding (which takes place during the 3 day waiting period).

Funding: Funds are then released to pay off all agreed upon loans and accounts. If you were receiving cash out of closing, the funds will be deposited within 2-3 business days.

The process is a no-brainer, since all borrowers are guided step-by-step through the process. But even though borrowers are familiar with playing the *Find The Money* game, they aren't up to speed on all the rules and strategies. They think the game's object is to find a loan with the lowest possible interest rate.

And most harried mortgage industry employees sometimes reinforce this misunderstanding because they don't take the time to explain the rules and strategies to their clients.

Instead of loan advisors, they are simply acting as loan order-takers!

Most people don't realize that the real goal of *Find The Money* is for them to get a loan at the lowest **overall** cost. That's right. Sometimes a higher interest rate will add up to greater savings when the fees and costs that are *incurred in each step* are factored in.

But that's not their only mistake…

Most people also don't realize that the players aren't really opponents. They just have different viewpoints of how the game is played. Both players have to win—enter into a loan contract—or neither one wins the game. The borrower wants to own the house. The lender wants to profit from the interest payments.

The Golden Rule

The Golden Rule—he who has the gold makes the rules—is never more obvious than when someone requests a loan. Companies lend money on their own terms, not what is convenient to the borrower. Their terms for lending are also known as conditions and guidelines.

Loan conditions are expressed by the length of loan, frequency of repayment, and the interest rate charged. A $200,000 loan for 30 years at 6% interest will be paid on a monthly basis. There are normally many more conditions, but those details vary from lender to lender.

Lending guidelines give the details for not just the way the money will be repaid, but also how 'safe' they feel about the borrower returning the money.

Safety is measured by the amount of risk a lender feels they are taking that money will not be paid back. The two major factors of risk are a borrower's ability to repay the loan and his history of repaying other loans. The final component of risk is verifying the collateral of the loan, the home itself.

Upfront Costs To Borrowers

Every loan has costs associated with it. Some lenders will advertise “no cost” loans but they are simply sacrificing upfront gains for long-term profits.

Why do they do this?

Lenders must make a profit. Otherwise, why play the game? Their view is, “You can pay me now, or you can pay me later.” Since most people are more concerned with the here-and-now, their immediate need, they focus on the out-of-pocket upfront costs of a loan, in particular, when refinancing.

After all, why should you pay $5,000 in closing costs to save $100 a month in mortgage payments? To answer that question, let’s assume you have a $195,000 loan @ 7% for 30 years. The payments are $1,299 per month. Today they have an opportunity to refinance the loan at 6%.

Don’t Get Blindsided By Upfront Costs

Most people don’t consider the *time value* of money. Assume for a minute that the closing costs for refinancing are $5,000. If they have $5,000 in the bank, most borrowers would like to keep it there. Yet with banks paying interest rates under 2%, at the end of a year they’d earn just $101 in interest.

So, being like most people, you also decide to add the closing costs to your loan balance. After all, a $200,000 loan @ 6% over 30 years will have a monthly payment of $1,199. Great! You’ll save $100 per month.

But if you were to pay $5,000 in closing costs, the payment on a $195,000 loan @ 6% would be $1,169.

That’s an additional savings of $360 per year.

If you subtract the $101 that you did not earn from bank interest, you still have a savings of $259 per year. And let’s not forget that you’d be paying taxes on the $101 you earned, so your saving would be greater.

Would you rather save $1,200 per year or $1,459 per year?

Saving $259 per year is a 5% return on your $5,000 investment, but let’s look 7 years down the road.

When you sell the home, and 95% of the population sells their house within 7 years, that $5,000 you spend will come back to you as long as you don’t sell your home at a loss. Let’s say you sell the home at $210,000.

	Out-of pocket Option	No out-of-pocket Option	
Loan Amount	$195,000	$200,000	
Loan Cost	$5,000	$0	
7 Years Savings	$10,213	$8,400	$1,813 Gross Savings
Profit from Sale	$15,000	$10,000	
Money Kept in Bank	$0	$5,750	Money earning 2% Interest
Net Amount	$25,213	$24,150	$1,063 Net Savings

Remember, leaving $5,000 in your savings account and earning 2% interest compounded annually will earn $750 after 7 years. That's a yield of 15% on your investment. **Tax fee!**

So moving $5,000 from a savings account into the equity of the house ultimately saves $1,063 over 7 years.

That's a 21% increase *on your $5,000 investment!*

So if you can manage to pay for some of your closing costs out-of-pocket, remember what a great investment it is.

Other upfront charges such as impound accounts and taxes are also often included in the borrowed amount. You will not see the same benefit for paying these fees out of pocket because they are not part of the loan. More about these fee later.

It often seems like borrowers are competing against one another for a lender's money. After all, they reason, there is only a finite amount of money, right. Yet this is not the case. Lenders have a seemingly infinite amount of money.

Why is that?

It is because it's not their money. They borrow it from somebody else! So borrowers need to recognize they aren't competing against borrowers. In order to get the best loan they are competing against the roadblocks and obstacles set up by lenders.

How Lenders Play The Game

Lenders view the game completely differently because money to them serves a dual role. The temporary use of their money is the product they buy and sell. They are money merchants who package "raw" dollars into "products" called loans. At the same time money is also used as a profit indicator.

The way they make a profit is to allow customers (the borrowers) to use their products (the money) for a set period of time (the loan term). Interest payments are their profit. *Profit Over Time* is when they'll actually see their profit.

Lender*s play Find The Money* only because they want to obtain new customers.

Dollars in Search of A Place To Call Home

Borrowers agree to exchange their own money for a lender's money over time by making regular payments to cover principal and interest.

The principal portion is for repaying the original sum. It is The interest portion is the additional money paid to compensate the lender for using the money over a period of time.

Is lending very profitable for lenders? Even at only 5.5% interest, over 30 years you'll repay over **twice** as much as you originally borrowed. I'll use this interest rate for illustrative purposes.

You can find amortization calculators all over the Internet if you're interested in the exact values But repayment schedules are computed in favor of the lender for the first half of the loan. In fact, after 15 years, a borrower has paid back a sum equal to the amount that was borrowed. Three fourths of the amount is applied to interest payments.

During the second half of the loan, 75% of the payments are applied toward repaying the loan and the remainder is applied to paying off the original loan amount.

For higher interest rates, even more than 75% will go toward interest during the first half of the loan.

The lender's goal is to create loan products with the least overall cost. But unlike other businesses where costs are incurred prior to the sale of a product, most costs are incurred after a borrower and lender reach an agreement, after *Find The Money* ends and the borrower and lender have "won."

How Lenders Think

At the core of approaches for keeping their costs down is the lender's view of risky. The cost of borrowing is set depending on how risky they consider lending money to a borrower.

One unbiased measurement is based predominantly on how the borrower has repaid loans in the past. It is quantified in a borrower's credit score. No wonder one of the first pieces of information a lender requires about a perspective borrower is their credit score.

Credit scores are obtained from credit reporting agencies. These agencies keep track of payment histories of borrowers as reported to them by various lending institutions.

Much like in golfing or bowling, which use a "handicap" system to enable competitors of unequal ability to have an equal chance to win, borrowers are assigned a "handicap" based on their historical record of loan repayment. Borrowers handicaps are called credit scores. The higher the score, the lower the risk a borrower is considered.

Another guideline lenders use to minimize risk is by making sure the borrower has enough income to repay the loan, and has a reputation for repaying loans. This is why lenders will make it more difficult to borrow when a person has suffered a job loss. They rightfully are concerned that the borrower will not have the ability to repay the loan.

Each lender develops descriptions and criteria of preferred borrowers—in terms if credit score and income—for particular loan amounts that have historically proven to be most profitable for the lender. These descriptions evolve into the loan products or loan programs they offer.

So the objective of *Find The Money* for borrowers is borrower to get a loan at the lowest overall cost. This is defined in terms of the interest rate and closing costs, possible prepayment penalties, impound account requirements, negative amortization, and other charges that may be contained in a loan.

Lenders objective is to minimize the risk that the loan will not be repaid. Examining credit scores, incomes, and other existing debt of borrowers enables lenders to calculate their risk.

If the borrower doesn't fit the mold set by a lender for one of their loan products, the game is over. Everybody loses. The borrower can't buy or refinance a home and the lender can't find a place to invest money.

A Limiting Move

The more you play the game, the better you get and the more familiar you are with the rules. Most people don't play the game too often. Some try to brush up on the rules themselves and run down to their local bank to play *Find The Money*. But the odds are not in their favor because the criteria used for qualifying borrowers and the programs offered to them are limited to the way that the institution plays *Profit Over Time.*

Borrowers Can Gain An Edge

Other borrowers believe that it would make sense to have a more advanced player of *Find The Money* help them win their game. These advisors are called mortgage brokers. Think of them as coaches for playing the game.

Mortgage brokers are familiar with the loan programs and programs offered by many lenders. They also have contacts and relationships with lenders that the average player of *Find The Money* does not. This fact alone gives them the edge for finding sources of funds at the lowest overall cost. But not all mortgage brokers are created equally.

What to Look For In a Mortgage Broker

First and foremost, make sure your broker is listening to you and understands what you want. Loans are like cars. Most everyone needs them, but it's even more important to find the right one. You wouldn't use a Lexus to haul around your sheetrock supplies, would you? A broker should be asking questions to determine what kind of loan will best suit your needs.

Second, make sure the mortgage broker has the time and energy to work on your loan. Don't you get frustrated when you're at a restaurant and you want a refill on your drink and the waitress is too busy taking orders for the tables all around you to recognize you have a request? That's the way some brokers will leave their clients feeling by not promptly returning phone calls or e-mail.

Finally, make sure your broker is keeping informed about the loan process and the costs of the loan. There is nothing worse than getting a call out of the blue and told to report to a closing the next morning, except showing up to sign the paperwork and being surprised that the closing costs or interest rate was higher than you were prepared to pay.

"It's not whether you win or lose, it's how you play the game."

Those words are never truer than when obtaining a loan. In this game, everyone wins if the borrower chooses the right loan. If you can't find the right loan for you, just keep searching for other lenders to play with who have programs that make more sense for your situation.

That's how to play the Mortgage Game, *Find The Money*.

We sincerely hope these tips and ideas will be of value to you. If we may be of any further service, please contact our office. We will consider it a privilege to be of service to you! If you would like a free consultation, call our office at 925-399-5359 or toll free at 866-822-8500.