Chapter 32: Understanding Homeownership

Key concepts for home buying and mortgages

KEY TERMS

Mortgage
A loan specifically for purchasing real estate, where the property serves as collateral

Down Payment
Initial upfront payment toward purchase price, typically 3-20%

Principal
The original loan amount borrowed to buy a home

Interest
The cost of borrowing money, expressed as a percentage

Escrow
Account managed by lender to collect and pay property taxes and insurance

PMI (Private Mortgage Insurance)
Insurance required when down payment is less than 20%, protects the lender

Home Equity
The difference between home's market value and amount owed on mortgage

TYPES OF MORTGAGES

Type	Down Payment	Best For
Conventional	3-20%	Good credit (620+), stable income
FHA	3.5%	First-time buyers, lower credit (580+)
VA	0%	Military/veterans
USDA	0%	Rural areas, income limits apply
Jumbo	10-20%	High-priced homes, excellent credit (700+)

Fixed-Rate Mortgage

Interest rate stays the same for entire loan term

- Predictable monthly payments
- Common terms: 15, 20, 30 years
- Higher initial rates than ARMs
- Best when rates are low

Adjustable-Rate Mortgage (ARM)

Interest rate changes after initial fixed period

- Lower initial rates
- 5/1 ARM = fixed 5 years, adjusts annually
- Risk of payment increases
- Best if moving/refinancing soon

PITI - MONTHLY MORTGAGE PAYMENT

P + I + T + I = Total Monthly Payment

P - Principal
Portion that pays down your loan balance

I - Interest
Cost of borrowing money

T - Taxes
Property taxes (held in escrow)

I - Insurance
Homeowner's insurance + PMI if applicable

TRUE COSTS OF HOMEOWNERSHIP

Upfront Costs:

- Down payment (3-20%)
- Closing costs (2-5%)
- Moving expenses
- Initial repairs/furniture

Ongoing Costs:

- Mortgage payment (PITI)
- Utilities
- Maintenance (1% of home value/year)
- HOA fees (if applicable)

Example: For a $300,000 home with 10% down:

- Down payment: $30,000
- Closing costs (3%): $9,000
- Total upfront: $39,000+
- Annual maintenance: ~$3,000

HOME BUYING PROCESS

1. **Financial Preparation** (6-12 months before)
   Improve credit, save for down payment, reduce debt
2. **Get Pre-Approved** (1-2 months before)
   Submit documents, get pre-approval letter
3. **House Hunt**
   Work with agent, view properties
4. **Make an Offer**
   Negotiate price, include contingencies
5. **Inspection & Appraisal**
   Professional inspection, lender appraisal
6. **Closing**
   Sign documents, pay closing costs, get keys

Benefits of Homeownership

- Building equity over time
- Potential appreciation
- Tax deductions
- Stability and control
- Fixed housing costs (fixed-rate)

Challenges of Homeownership

- Limited liquidity
- Market risk
- Maintenance burden
- Reduced mobility
- Unexpected repair costs

FINANCIAL READINESS CHECKLIST

Factor	Recommended
Credit Score	620+ (conventional), 580+ (FHA)
Debt-to-Income Ratio	Below 36% (ideally)
Down Payment	3-20% saved
Emergency Fund	3-6 months expenses (separate)
Employment History	2+ years stable income
Geographic Stability	Plan to stay 3-5+ years

Key Takeaway: Homeownership is a major financial decision that requires careful consideration of your finances, lifestyle, and market conditions. Understanding all costs beyond the purchase price and ensuring you're truly ready will help you make a decision that aligns with your long-term goals.