

Too much house for your income?

We often hear the phrase, “bigger is better.” In fact, according to the *LA Times*, between 1975 and 2005, the average size of a new American single-family house grew by 48 percent, even though the average household size fell from 2.94 to 2.6 people. While bigger homes are a recent trend, it’s important to be sure you don’t buy more house than you need and undermine your financial security in the process.

Don’t get caught in a debt trap

Here are a few tips to help you decide how much is too much for you and your home financing:

- **Ask yourself “why to buy”** Do you really need more space? How many square feet of living space does your family really need?
- **Never assume more than you can pay off each month.** Generally, there are only three things worth going into debt for: education, transportation and housing. Still, you need to compare your income with what a mortgage (combined with your other expenses) will mean in “out go”.
- **Beware of balloon payments.** Avoid mortgages that entice you with artificially low “teaser” rates, or minimum payments that apply for only a short period of time before they increase dramatically.

Assessing your debt circumstances

A quick evaluation of your debt-to-income ratio can tell you if you’re in too deep. Financial advisors recommend keeping your total debt payments under 36 percent of your pretax income.

To figure this ratio:

1. Total your monthly debt payments. Include total house payment, car loans, student debt and credit cards.
2. Take your total annual salary, including bonuses, and divide by 12 to determine your pretax monthly income.
3. Divide your monthly debt by your pretax monthly income.

What your ratio says:

- Under 20 percent: No problem.
- 20-36 percent: A good debt load for most people.
- 37-43 percent: Your debt levels are a little high.
- Over 43 percent: Your debt levels are definitely higher than recommended

How to lower your ratio.

Too high a ratio could influence your ability to deal with rainy-day emergencies such as an unexpected lay-off, and extended illness or a drop in business. The New Year is a good time to make a plan for getting your finances in line with your income by reducing your overall debt levels, especially those with variable rates.

There are several ways to do so. Two possibilities that can result in a quick change are (1) to find a home that is a good financial fit; (2) to explore your refinance potential.

(1) Downsize. Consider trading down to a smaller home. This could be a blessing in disguise. A smaller home may actually feel cozier and may be easier to maintain and insure. (See my article on “Right-Sizing for more on this subject.)

(2) Reduce your rates. Look for opportunities to refinance home loans at lower rates. Coldwell Banker has developed a full line of mortgage loans to fit any situation.

For more help:

Email me should you need some help in deciding your proper debt level or are looking to find just the right home to meet your financial scenario.