How to Get a Loan with a High Debt-to-Income Ratio

Getting a home loan with a high debt-to-income ratio is possible

Buying a house with a high debt-to-income ratio is possible but it can be more challenging.

When you apply for a mortgage, the lender will make sure you can afford it. Doing so involves comparing your debts and your income — formally called your **debt-to-income ratio, or DTI**.

If your DTI is too high, you could have a hard time getting approved for a home loan. However, there are ways to make the numbers work, even with a higher DTI.

What is debt-to-income ratio (DTI)?

Debt-to-Income (DTI) ratio is a financial measure that lenders use to evaluate a borrower's creditworthiness and ability to manage monthly payments and repay debts.

It compares your total monthly debt payments to your gross monthly income, expressed as a percentage. This ratio helps lenders assess your financial health and your capacity to take on and manage new debt, such as a secured loan or home equity loan.

Lenders want to be sure that prospective homeowners aren't taking on more debt than they can manage before approving their mortgage loan application. When a borrower applies for a home loan, mortgage lenders consider two types of debt-to-income ratios.

Front-end DTI

Front-end DTI is limited to housing expenses and includes your potential monthly mortgage payment, homeowners insurance premiums, and property taxes.

Lenders often prioritize multiple factors in mortgage applications, with the front-end ratio receiving relatively less attention, except in specific

cases like FHA loans. Nevertheless, your debt-to-income ratio serves as a useful gauge to assess your financial situation and determine a realistic affordability range for purchasing a home.

Back-end DTI

Back-end DTI is more commonly used during a home loan application because it provides an overall view of your creditworthiness and monthly financial wellbeing.

Your back-end ratio looks at all of your recurring monthly minimum payments, including the front-end DTI plus any monthly debt from credit cards, student loan payments, debt consolidation loans, auto loans, and personal loans.

Your debt-to-income ratio typically doesn’t include basic household expenses or monthly bills for utilities, groceries, dining out, and entertainment. Instead, the types of debt DTI focuses on are minimum monthly payments from lines of credit that are regular and recurring.

How to calculate debt-to-income ratio

Understanding your DTI is important to managing your financial health, especially if you’re dealing with current debt, considering new credit, or looking to qualify for a home loan with high DTI.

Here’s how to calculate your DTI:

- **Total monthly debt payments:** This includes all your monthly debt obligations — such as credit card payments, car payments, student loans, personal loans, debt consolidation loans, and any other recurring debt that you have. It does not typically include variable expenses like utilities, groceries, or insurance.
- **Gross monthly income:** This is your total monthly income before taxes and any other deductions. It includes your salary or wages, bonuses, commissions, and any other sources of income you may have, like rental income, child support, or alimony.

The DTI ratio is calculated by dividing your total monthly debt payments by your gross monthly income. For example, if your monthly debt payments total $2,000 and your gross monthly income is $6,000, your DTI ratio would be 33.3%.

- Monthly debt payments / monthly gross income = X * 100 = DTI ratio

Lenders use the DTI ratio to gauge how much additional debt you can handle and still comfortably meet your financial obligations. A low DTI ratio generally indicates healthier personal finances, as it suggests that a smaller portion of income is allocated towards debt payments.

What's the maximum debt-to-income ratio for a home loan?

The maximum debt-to-income ratio for a home loan can vary depending on the lender and the type of loan you're applying for. Generally, lenders prefer a DTI ratio of 43% or lower because it indicates that you have a good balance between debt and income, making you a less risky borrower.

This means your total monthly debts, including your prospective mortgage and any other debts like car payments or credit card bills, shouldn't exceed 43% of your monthly income.

However, some loan programs, like those backed by the Federal Housing Administration (FHA), may allow DTI ratios higher than 43%, sometimes up to 50% or slightly more, especially if you have compensating factors such as a high credit score or substantial savings.

- **Conventional loans:** Typically require a DTI ratio of 43% to 45%. Lenders might allow higher ratios, up to 50% for applicants with good credit history or substantial cash reserves.
- **FHA loans:** Offer more flexibility with DTI ratios, allowing up to 50%. These loans are designed to accommodate borrowers with minimum credit scores of 580, providing a pathway to homeownership with more lenient eligibility requirements.

- **VA loans:** Do not specify a maximum DTI ratio, though borrowers with higher DTIs may face additional scrutiny. Some lenders are open to ratios as high as 60%, particularly for veterans and surviving spouses, reflecting the program's accommodating stance.
- **USDA loans:** Designed for home buyers in eligible rural areas, these loans permit DTI ratios of up to 46%. Applicants must also meet household income limits, not exceeding 115% of the median income for their area.

How to get a loan with a high debt-to-income ratio

A high debt-to-income ratio can result in a turned-down mortgage application. Luckily, there are ways to get approved even with high debt levels.

1. Try a more forgiving loan program

Different programs come with varying DTI limits. For example, Fannie Mae sets its maximum DTI at 36% for those with smaller down payments and lower credit scores. Often, the limit for those with higher down payments or credit scores is 45%.

FHA loans, on the other hand, allow a debt-to-income ratio of up to 50% in some cases, and your credit does not have to be top-notch.

Likewise, USDA loans are designed to promote homeownership in rural areas — places where income might be lower than in highly populated employment centers.

Perhaps the most lenient of all are VA loans, which are zero-down financing reserved for current and former military service members. If there is a lot of **residual income**, the DTI for these loans can be quite high. If you're fortunate enough to be eligible, a VA loan is likely the best option for high-debt borrowers.

2. Restructure your debts

Sometimes, you can reduce your ratios by refinancing or restructuring debt.

Student loan repayment can often be extended over a longer period of time. You may be able to pay off credit cards with a personal loan at a lower interest rate and payment. Or refinance your car loan to a longer term, a lower rate, or both.

Transferring your credit card balances to a new one with a 0% introductory rate can lower your payment for up to 18 months. That helps you qualify for your mortgage and pay off your debts faster as well.

If you recently restructured a loan, keep all the paperwork handy. The new account may not show up on your credit report for 30 to 60 days. Your lender will need to see new loan terms to give you the benefit of lower payments.

3. Lower your loan amount

Sometimes, simply adjusting the loan amount you're applying for can improve your DTI ratio by reducing how much of your income is viewed as committed to debt each month. It's like choosing a less expensive item to keep your budget in check.

You can bring your debt-to-income ratio (DTI) within acceptable limits by opting to buy a less expensive home and, therefore, a smaller mortgage. This might involve revisiting your housing needs and budget to find a balance that works for both you and potential lenders.

4. Pay down the right accounts

If you can pay an installment loan down so that there are fewer than 10 payments left, mortgage lenders usually drop that payment from your ratios.

Or you can reduce your credit card balances to lower your monthly minimum.

You want to get the biggest bang for your buck, however. You can do this by taking every credit card balance and dividing it by its monthly payment, then paying off the ones with the highest payment-to-balance ratio.

Suppose you have $1,000 available to pay down the debts below:

Balance	Payment	Payment-to-balance ratio
$500	$45	9.0%
$1,500	$30	2.0%
$2,000	$50	2.5%
$3,000	$150	5.0%

The first account has a payment that's 9% of the balance — the highest of the four accounts — so that should be the first to go.

The first $500 eliminates a $45 payment from your ratios. You'd use the remaining $500 to pay down the fourth account balance to $2,500, dropping its payment by $25.

The total payment reduction is $70 per month, which in some cases could turn a loan denial into an approval.

5. Cash-out refinancing

If you're trying to refinance but your debts are too high, you might be able to eliminate them with a cash-out refinance.

The extra cash you take from the mortgage is earmarked to pay off debts, thereby reducing your debt-to-income ratio.

When you close on a **debt consolidation refinance**, checks are issued directly to your creditors. You may be required to close those accounts as well.

6. Get a lower mortgage rate

One way to reduce your debt-to-income ratio is to drop the payment on your new mortgage. You can do this by "buying down" the rate — **paying points** to get a lower interest rate and payment.

Shop carefully. Choose a loan with a lower start rate, for instance, a 5-year adjustable-rate mortgage instead of a 30-year fixed loan.

Buyers should consider asking the seller to contribute toward closing costs. The seller can buy your rate down instead of reducing the home price if it gives you a lower payment.

If you can afford the mortgage you want, but the numbers aren't working for you, there are options. An expert mortgage lender can help you sort out your debts, tell you how much lower they need to be, and work out the details.

Tips to get a loan with a high debt-to-income ratio

Before you apply for a mortgage, there are a few strategies you can use if your debt-to-income ratio is high.

Increase your income

Boosting your income is a practical approach to lowering your DTI ratio. Consider exploring opportunities like a side job, additional hours at your current workplace, or freelance work. Remember, lenders often prefer to see a consistent income history, typically around two years, for each source of income. This increase can significantly help in reducing your DTI, especially when applying for mortgages that cater to high debt-to-income ratios.

Tackle your smallest debts first

An effective method to reduce your DTI is by focusing on your smaller debts. Paying off these debts entirely, if feasible, can lead to an immediate decrease in your DTI. Alternatively, consistently paying more than the minimum required amount on these debts can gradually reduce your DTI. This approach is especially beneficial for those

exploring high DTI loans or mortgages from lenders who are considerate of high debt-to-income ratios.

Consider adding a co-borrower

Involving a spouse or partner in your loan application can be advantageous. If your partner has a lower DTI, their financial profile can help reduce the overall DTI for the household. This strategy is particularly useful for couples seeking high debt-to-income ratio mortgage solutions. However, if your partner's DTI is similar to, or higher than yours, their inclusion might not be beneficial.

Opt for a co-signer

For those aiming to secure a mortgage with a high DTI, enlisting a co-signer, like a family member or a close friend, can be a viable option.

A co-signer's financial stability and debt-to-income ratio are considered by lenders, which can enhance your loan application. This could potentially lead to qualifying for a larger mortgage or obtaining more favorable terms, such as lower interest rates. It's important to note that a co-signer doesn't need to reside on the property but must agree to fulfill the loan obligations if you are unable to do so.

FAQ: Getting a loan with a high DTI ratio

What is a good debt-to-income ratio?

While lenders and loan programs all have their own DTI requirements, typically a good DTI is 36% or lower.

What happens if my debt-to-income ratio is too high?

Borrowers with a higher DTI will have difficulty getting approved for a home loan. Lenders want to know that you can afford your monthly mortgage payments, and having too much debt can be a sign that you might miss a payment or default on the loan. If you're in this situation, try to pay down or restructure some of your bigger debts before applying for a home loan.

How to lower your debt-to-income ratio?

To lower your debt-to-income (DTI) ratio, prioritize paying off existing debts and refrain from incurring new debt, especially if you have bad credit. Consider strategies such as setting aside additional money for credit card debt, budgeting to better control housing costs, and consolidating debt to get lower interest rates. Simultaneously, explore opportunities to increase your income through avenues such as seeking a raise, working overtime, or taking on additional part-time work. By simultaneously reducing debt and boosting income, you can effectively decrease your DTI ratio, improving your financial situation and home loan eligibility.

Debt-to-income vs credit utilization?

Some home buyers may confuse debt-to-income ratio with credit utilization ratio, also known as debt-to-limit ratio and debt-to-credit ratio. Your credit utilization ratio shows how much of your available credit (credit limit) you're using. As an example, if you have a $100,000 credit limit across several credit cards and your current balance is $5,000, then your credit utilization ratio is 5%.

A high debt-to-income ratio can make it tougher to get a home loan. Fortunately, lenders have some flexibility when it comes to mortgage requirements.

If your DTI is high but you're a reliable borrower in other respects, there's a good chance you could still qualify. To find out, talk to a local lender and check your eligibility today.