MANNY MOSQUERA
FOR MORTGAGES

WHAT IS THE DIFFERENCE BETWEEN CONVENTIONAL AND FHA LOANS?

Consumers qualify for various types of mortgages based their financial situations. Typically, people with a more solid financial footing usually qualify for Conventional mortgages. These are loans that are ensured by either Fannie Mae or Freddie Mac. People who are just starting out in their adult life or have a little more debt than they would like or have credit that could use some improvement typically would be best suited for a government-insured mortgage such as those offered by the Federal Housing Administration (FHA).

Making sure that you understand the benefits and shortcomings of the different mortgage programs that are available is extremely important. You will want to ensure that you are choosing the right program for you and your family is that this is a loan that you will likely have for quite some time.

Conventional Mortgages

Conventional loans can be riskier for lenders since they are not insured by the Federal Government. It is because of this reason that lenders make sure they are only giving these loans out to people who are in a strong and stable financial position. Typically speaking these loans also have slightly higher interest rates.

Allowable down payments for these loans can be as little as 3%. You can also put down as much as you are financially able to. Down payments of 20% or more eliminate the borrower from having to pay private mortgage insurance (also known as PMI). If you are required to pay PMI, you will only need to do so until the day that you have 22 % equity in your home. How quickly your equity grows will be determined by how fast you pay down your loan, and how quickly your home appreciates in value.

Should you be required to pay PMI with you Conventional loan the cost of your PMI will be based on how good your credit is. The higher your credit score is the cheaper your monthly PMI costs will be.

A good credit standing is also important to be eligible for a Conventional Loan. The required minimum credit score is 680. No open collections, judgments or disputes are allowed. If you do have any of these on your credit it is important to have these rectified early on so that your Loan Officer has time to work with the credit bureaus to have them updated or removed.

Strict debt to income ratios can be expected with a Conventional Mortgage. Higher income/lower debt or any variation of the above will be required to qualify. Exactly what the maximum debt to income allowances are will vary based upon credit score, how much of a down payment you plan to put down and whether your loan will be insured by Fannie Mae or Freddie Mac.

FHA Mortgages

These loans are government insured. This is important to know for a number of reasons. To start with they typically have cheaper interest rates. They can also be easier to qualify for due to looser guidelines. The intention is to make the American dream available to everyone.

The minimum down payment required for these loans if 3.5% of the purchase price.

FHA is much more lenient with regards to credit. The ideal credit score for these loans would be 640. There are some lenders that will accept scores down to 580. It is important to note that if your scores are below 640 but still happen to meet the 580 requirements it would be a great idea to see how you can improve your scores to get at least to the 640 level. Below 640 fico scores will result in a higher rate and the lender will further tighten the allowable debt to income levels. As a result, you will qualify for less. Spending a little time repairing your credit can be well worth the effort.

Understanding how private mortgage insurance (also known as PMI) works on an FHA loan can be confusing.

FHA loans have monthly PMI just as Conventional loans do. But FHA loans structure the PMI very differently. If a person puts 10% or more as a down payment they are required to PMI for 11 years. If a person puts down less than 10% they are required to pay PMI for the life of that loan. Providing your loan does not have a Pre Payment Penalty then there is no requirement that dictates how long you must keep this loan.

Many people purchase their homes using an FHA loan to take advantage of FHA's loose guidelines. And then years down the road when their financial situation is stronger and they have paid down a significant amount of their mortgage they can refinance out of their FHA loan into something more desirable like a Conventional loan.

In addition to the monthly PMI, there is also upfront PMI, also known as MIP. This is only associated with FHA loans. MIP is financed into your mortgage and paid off through the life of the loan. The amount of this MIP will vary based on loan sizes, terms and down payment.

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