The Essential Guide for

First-Time Home Buyers

Success Starts Here.

First State Community Bank

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1. Introduction

Buying a home is a major milestone and an exciting process. Owning your own home can bring a sense of satisfaction, pride, and security. Once you buy a property, that home is yours and you get to make it your own. You also may enjoy many tax benefits and take comfort in knowing that real estate value tends to appreciate over time.

When you decide it’s finally time to take the plunge and buy a home, the first thing you will probably do is look online at Zillow, Realtor.com, and other online property listings to see what is available in the area you want to live. The second thing you are going to do is start looking into mortgages to determine what you can afford and how monthly homeowner expenses are going to affect the family budget.

Once you buy a property, that home is yours and you get to make it your own.

There are a lot of steps and details that go into buying a home, and the more you know about the process up front, the more confident you will be when making each decision along the way. Throughout the process, you will deal with real estate agents, mortgage bankers, home inspections, taxes, property appraisals, and more. In addition, your finances will be reviewed to determine if you are qualified to borrow enough money to buy the home you want.

With a deep understanding of your finances and clarity on the ins and outs of the home buying process, you’ll be equipped to ask better questions, make confident decisions, and purchase the home that’s perfect for you.

2. How Much Home Can You Afford?

The first step for most people is research. With help from the web, you can now research specific areas and learn most of what you need to know, such as the quality of the schools, local taxes, cost of living, and the going price for properties. If you have an area or neighborhood in mind that is close to work or near family and friends, then take a look at home prices and see how much house you can get for your money.

When considering what you can afford, you have to think about your overall household budget and how much you are paying for housing now. The generally accepted rule is that you want to commit 25 percent[1] of your monthly take-home pay to your mortgage payment. Although 25 percent is the conservative estimate, some home buyers are taking on mortgages closer to 35 percent[2] of their after-tax income. The most important consideration is to plan for the future and factor in how your income will change over time.

Although **25 percent** is the conservative estimate, some home buyers are taking on mortgages closer to **35 percent** of their after-tax income. The most important consideration is to plan for the future and factor in how your income will change over time.

The best way to calculate what you can afford is to start with a comprehensive household budget. Itemize all the money you spend in a month and determine how much you can reasonably allocate for a mortgage. Be sure to account for all your debt, including student loan debt. When you add up your household debt from your credit cards, student loans, homeowner's policy, and mortgage payment, be sure your debt does not exceed 42 percent of your income. Use a mortgage calculator to help you determine what you will have to pay.

Also, be sure to account for all of your household costs. In addition to the mortgage, you will need to pay for home maintenance and improvements—and don't forget property taxes. When you own your own home and a pipe bursts or your refrigerator stops working, you can't call the landlord; you are the landlord, so you need to be prepared to pay for repairs.

The good news is that as a first-time home buyer, you can often receive incentives from banks and mortgage lenders to get you started. Though most home purchases require a down payment of 20 percent of the home price, many banks offer mortgages with 0 percent down for qualified buyers. Of course, the more money you can put down on a new home, the more equity you have in the house and the lower your mortgage payments will be. If you are even thinking about buying a home, start putting aside money now. Open a savings or money market account and put money aside until you are ready to buy.

In addition to determining how much home you can buy and how large a down payment you need, you also need to consider the type of mortgage that best suits your lifestyle. There are different types of mortgages, each with its own unique structure, benefits, and disadvantages.[4] Here are the five most common types of mortgages:

Fixed rate mortgage – As the name implies, this is a mortgage that has the same interest rate for the duration of the mortgage. The interest rate is based on current market rates and the mortgage is usually paid over 15-30 years.

Adjustable rate mortgage (ARM) – An ARM changes its interest rate to match the current market rate after an initial period of 1-5 years. After the initial period of fixed-rate interest, the ARM interest rate will adjust annually, going up or down depending on current mortgage interest rates.

Construction mortgage – A construction mortgage is for new home builds and consists of two parts: a loan for actual home construction and a mortgage on the completed home. The advantage for new home construction is that it is one loan that covers construction and home ownership costs. Be sure you understand the terms and restrictions of a construction loan before you sign.

Jumbo loans – A jumbo mortgage exceeds the lending limits of a conventional loan established by Fannie Mae and Freddie Mac, which means the lender is taking a larger risk to lend more money. You need excellent credit to qualify for a jumbo loan.

Government-insured mortgages – Conventional loans are backed by the bank or lending institution. However, there are also government-insured loans available from the Federal Housing Administration (FHA loans), the U.S. Department of Veteran Affairs (VA loans), and the U.S. Department of Agriculture, which are managed by the Rural Housing Service (USDA/RHS loans).

Your bank loan officer will help you determine the best loan for you. You will never truly know how much you can afford until you prequalify for a mortgage.

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3. Applying for a Mortgage

Before you get serious about finding a new home, you should arrange for financing. Having prequalification for a mortgage is essential, especially in a competitive real estate market. Once you find the perfect property, you need to be prepared to make an offer right away; if you have to delay to get your financing in order, someone who is ready to buy will close the deal first.

To get prequalified, talk to your bank or mortgage lender and review your mortgage options. Be prepared to provide the lender with details about your finances, including your income, your debt, and your assets. Most mortgage prequalification can be done by phone or online at no cost. It typically takes 1-3 days to get a prequalification letter.

4. Finding a Real Estate Agent

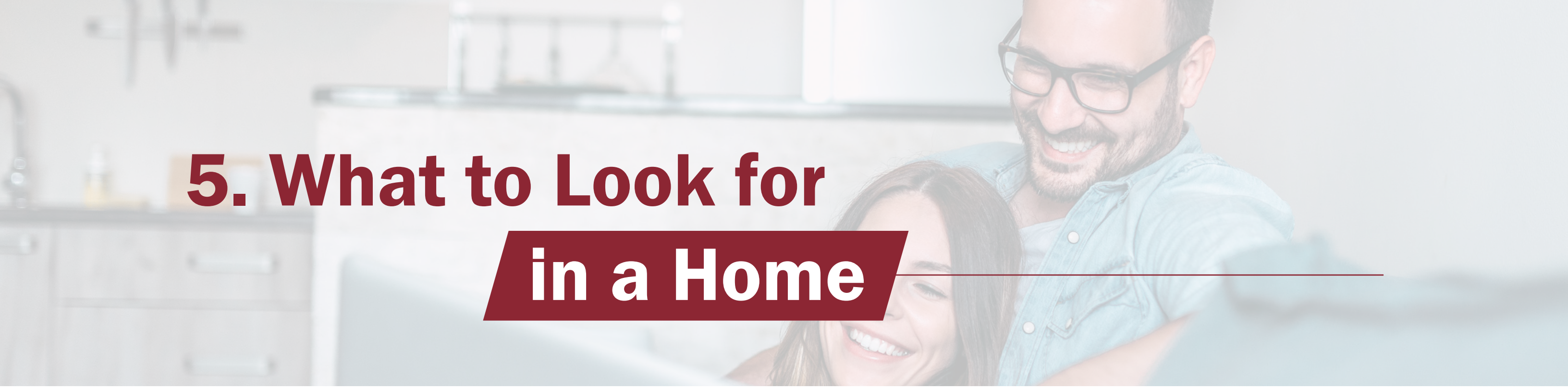
Once you have been preapproved for a mortgage, you are ready to start house hunting. Although there are many online tools that may help you find attractive properties, you will still need an experienced real estate agent to help you find the right home and negotiate the sale.

The real estate agents job is to help you, as a prospective home buyer, find the right property and finalize the transaction.[8] A good real estate agent will listen carefully to your requirements and what you want in a home, and then advise you on potential regions and properties that may match your needs. You should feel free to be open with your real estate agent about your financial plans and hopes for the future, as well as other needs that may affect your buying decision, such as commuting distance or finding the right school district. Working with a real estate agent should be a collaborative experience; they shouldn't try to "sell" you just to make their commission fee.

When looking for the right real estate agent, you want to find someone who knows the market and is familiar with the area; they will know about potential properties you won't see online. You also want someone with a strong sales track record, so be sure to ask for referrals. Most of all, you want someone trustworthy. Personal referrals are a great way to start looking.

Once you are ready to start looking, bear in mind that it will take a while to find the right home. Most first-time home buyers look at an average of 10 homes over 10 weeks.

You also want someone with a strong sales track record.



5. What to Look for in a Home

Now that you have a real estate expert in your corner, it's time to start looking at homes. The first rule of house hunting is try not to fall in love. Buying a home is a big decision, and making the wrong choice can be extremely costly. Even if the house is exactly what you want, don't let your enthusiasm overshadow practical considerations such as the down payment, taxes, maintenance costs, and other factors that could shatter your budget. Shop with your head as well as with your heart.

When assessing a possible home, consider how it fits your family's needs and your lifestyle. You want to make sure there are enough bedrooms and bathrooms, especially if you are starting a family. Do you need a yard for pets and/or children? Do you need a garage and is there adequate parking available? Do you know how much upkeep the house will need? Try to envision living in that house and consider all the pros and cons.

As you walk through the property, there are any number of red flags to look for.[10] Use all your senses when looking at a house. Here are some tips:

1. **Be wary of unidentified smells.** If the seller has scented candles lit and fresh cookies baking, ask yourself what they are trying to cover up.
2. **Check the flooring.** Loose bath tiles may be a simple do-it-yourself fix, but warped floorboards or soft floors may indicate a bigger issue.
3. **Check the foundation.** Older homes can develop foundation problems. Small cracks may indicate normal settling, but bigger cracks could mean a real problem. Also, look for level windows that open easily and level floors. Rolling a marble will tell you if the floors are level.
4. **Consider water worries.** In addition to looking for water damage, check to be sure there isn't a risk of flooding in heavy rains.
5. **Look for worn-out windows.** If windows stick or have chipped putty, it may mean they need to be replaced.
6. **Look for mildew and mold in the kitchen and bathroom.** This could be caused by poor cleaning, or it could be more serious. A home inspector should be able to tell you if there is a mold problem.
7. **Identify poor ventilation.** If there is condensation on the windows, discolored walls, or peeling paint, it could be an indication that moisture is trapped in the house.
8. **Keep an eye out for deferred maintenance.** If the house has not been maintained, make sure you know what you can expect in the way of repairs. In addition to adding a coat of paint and fixing a leaky faucet, you may have to deal with problems such as a poorly maintained water heater, a chimney that has never been cleaned, or a leaking roof.

When looking at any house, don't be afraid to ask questions. If something looks odd or out of place, ask about it. Once you find the right property and are ready to make an offer, know that the seller accepts your offer, you will need to follow up with a home inspection. A home inspection is part of the buying process and should uncover any issues, and many lenders require an inspection before they will approve a home loan.

The home buyer usually hires a home inspector to visually inspect the property prior to the closing, although it is becoming more common in competitive markets for the seller to provide an independent home inspection report to expedite the sale. Even if the seller provides such a report, you should still have your own inspection done. The home inspector will review every aspect of the house, including the structure, foundation, roof, electrical wiring, plumbing, heating, and air conditioning, and ensure that the property has the proper safety features and complies with the building code. Note, however, that this is a visual inspection and a home inspector will not necessarily find every issue.

Once you have the home inspection report, you will have a more accurate sense of the kinds of repairs or improvements you may want or need to make to the home. To avoid buyer's remorse, this is when you need to take a hard look at your prospective new home, your budget, and your plans for the future.

The home inspector will review every aspect of the house.

For example, can you afford any renovations or necessary updates? What about monthly household costs such as heating and cooling, water, electricity, and so on; do they fit your budget? How long do you plan to live in the house? Will you likely earn more money in the future? What about changing locations as part of career advancement? Have you considered likely resale costs? Try to address all the possible variables and concerns before you proceed with the sale.

Once you decide you have found the right home for your family and your lifestyle, it's time to close the deal. If the inspection revealed that there are issues that need to be addressed or repairs that need to be made, work with your real estate agent to come up with a final offer that factors in the repair costs. The seller may choose to arrange and pay for the repairs themselves, or they may consider lowering the sale price of the house.

When buying your first home ...

1. Try not to fall in love right away (the wrong home purchase will break your heart as well as the bank).
2. Buy for the future as well as today.
3. Negotiate—don't expect to pay the listing price.
4. Do a thorough and careful home inspection.
5. Don't rush into making a decision because you feel pressured—there is always another house.
6. Remember to factor closing costs and other unexpected expenses into your budget.

6. Time to Close Escrow

Once you finalize your financing, it's time to close on the house, also known as escrow.[11] During escrow, the title to the house changes hands, you finalize the mortgage, and the seller receives the funds from the sale.

An escrow agent, usually a title company, is hired to handle the transaction. The title company serves as a neutral third party that holds the paperwork and funds in trust until the transaction is complete. The title company ensures that the title of the home is free of encumbrances, such as liens, and ready to transfer.

This is also when you remove any contingencies, such as having a mortgage, completing an inspection, an appraisal (which will be required by the mortgage lender), any repairs agreed to prior to the sale, and a final walkthrough. Each contingency typically has a time limit, so work with your real estate agent to make sure they are removed. If you miss a deadline, you can't enforce that contingency as part of the sale.

As part of closing, you also will need title insurance, homeowners insurance (also required by the lender), home warranties, and possibly mortgage insurance. You should be prepared to pay for closing costs as part of the sale. The national average for closing costs is 2-5 percent of the purchase price, but you won't know the exact cost of closing until right before you sign the final paperwork.[12] The closing costs can be shared by the buyer and seller, but be prepared to have a cashier's check for your share when you close escrow.

Congratulations! You have just purchased your first home. The home buying process has a number of steps, but remember, you don't make this journey on your own. Your most important guides in the home buying process are your mortgage lender and your real estate agent. Look for professionals with a proven track record whom you can trust.

At First State Community Bank, we have been helping first-time home buyers for more than 60 years. We are committed to helping every customer achieve financial success, and that includes buying their first home. We offer a wide range of mortgage products at competitive rates designed to suit every financial situation. If you are thinking about buying your first home, the mortgage experts at First State Community Bank are ready to offer their expertise to help you make the right home loan choice.

If you miss a deadline, you can't enforce that contingency as part of the sale.

Glossary

For First-Time Home Buyers

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A

Adjustable rate mortgage (ARM) – A mortgage whose interest rate is applied to the outstanding balance on the home loan and changes or adjusts periodically, usually monthly or annually, to reflect current market interest rates.

Appraisal – An independent assessment of the value of a property offered by a licensed appraiser. Appraisals on homes are required prior to obtaining a mortgage.

C

Conventional loan – A mortgage that is not guaranteed by any government agency, such as the FHA.

D

Down payment – The initial payment required from the buyer for a purchase of an expensive item, such as a car or a house. For first-time home buyers, the minimum down payment can range from 0-20 percent of the purchase price.

E

Equity – The current market value of a house or property minus any liens such as an outstanding mortgage balance. The equity in a home will change over time based on market conditions and the outstanding mortgage balance.

Escrow – The temporary condition when an item such as property is transferred to a neutral third party as part of a sale. The property and monies are held in trust until the terms of the transaction are complete.

F

Fannie Mae – The nickname for the Federal National Mortgage Association, which was established in 1938 to create a secondary mortgage market. Fannie Mae is now a federally chartered corporation that buys mortgages not insured by the FA.

Freddie Mac – A government-owned corporation that purchases mortgages and packages them as mortgage-backed securities. Banks use Freddie Mac funds to give loans to home buyers.

Federal Housing Authority (FHA) – A United States government agency created by the National Housing Act of 1934. The FHA is responsible for setting standards for home construction and underwriting and insuring loans made by private lenders for home building.

Fixed-rate mortgage – A fully amortized mortgage whose interest rate remains the same through the term of the loan.

H

Home warranty – A residential service contract to maintain home appliances such as washers, dryers, water heaters, air conditioning, furnaces, and so on.

Home warranty insurance – Insurance protection for things that might happen to your home because of fire, theft, natural disaster, and so on. It differs from a home warranty.

J

Jumbo loan – Financing that exceeds government limits and, unlike a conventional mortgage, is therefore ineligible to be secured by Fannie Mae or Freddie Mac.

L

Loan principal – The amount of a mortgage or loan that is still owed by the borrower before interest.

M

Money market account – An interest-bearing bank account that typically pays a higher interest rate than a savings account and that offers limited check-writing ability.

Mortgage broker – An intermediary who matches mortgage borrowers and lenders but does not fund the mortgage themselves. For a commission fee, the mortgage broker gathers the necessary paperwork from the borrower and shares with the mortgage lender for loan approval.

Mortgage interest rate – The rate of interest or percentage charged for a mortgage. The mortgage interest is the money charged for the home loan and is paid along with the principle as part of monthly payments over the life of a mortgage.

P

Prequalify – Using information submitted by the borrower, a bank or mortgage lender provides an estimate of how much you are able to borrow. It is not a guarantee that they will give you a mortgage.

T

Title insurance – A form of indemnity insurance against financial loss in the event there is a problem with the property title after financing.

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Introducing the First-Time Homebuyers Savings Account

Owning your first home is easier than you think.

If you're ready to take the leap from renting to homeownership but unsure where to start, we can help. Learn more about this program below.

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