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How Much Down?

Once upon a time you had to have 25% down to qualify for a mortgage. Then Canada Mortgage and Housing Corporation (CMHC) decided that was too high a hurdle, and told people if they were willing to pay mortgage insurance, they could get into a home for 10% down. Since the mortgage insurance was paid upfront to CMHC, and simply incorporated into the mortgage where the borrower couldn't feel the pain of the insurance premium, this worked very well for both borrowers and lenders alike.

CMHC, again, in an effort to making housing affordable to Canadians, lowered the minimum downpayment to 5%. Whoo-hooo. More people bought. Then CMHC lowered the minimum downpayment to zero and a whole mess of people decided to jump into the housing market, ponying up substantial insurance premiums. Lenders loved it too.

If you buy a home with anything less than 20% down, you're going to have to buy high-ratio mortgage insurance. This **mortgage insurance premium** is calculated as a percentage of the loan amount, and the percentage depends on the loan to value ratio.

The higher the loan-to-value ratio, the higher the premium cost. In other words, the lower your downpayment, the more expensive the insurance. While this premium may be paid in cash, nobody does this, so it is added to the mortgage amount and amortized over the period you've chosen.

On a $200,000 house with no money down, the mortgage insurance would be 3.1 percent of the value of your home or $6,200. Added into your mortgage, that mortgage insurance premium would end up costing you $13,605 if you amortized for 25 years, or $19,330 if you amortized for 40 years.

So how much downpayment should you have? Well, if you don't want to pay mortgage insurance, you'll need at least 20% down. And if you want to buy more house than your income can support, a bigger downpayment would help.

Let's say you figure out you can afford a home valued at $178,000 based on your income with nothing down. If you managed to save $36,000 for a downpayment, then you could look at homes in the $214,000 range. The bigger the downpayment, the more house you can buy on the same income.

But, you say loudly, if I don't have a very big income, how am I to save a whopper of a downpayment? Good question.

> Do you have assets you can sell? A car? What's more important, the car or owning a home? Own a boat?
>
> How about investments like stocks or bonds or mutual funds? Sell 'em and bank the cash.
>
> Consider saving your tax refunds. Make a contribution to an RRSP and the tax man may give you some money back that you can use to increase your downpayment.
>
> Use the **RRSP Home Buyer's Plan**.

Talk your parents/grandparents into helping you.

Ask for cash (to build your savings) for every birthday, or other special event, until you own your own home.

Ask for a raise and then sock away the difference in your income in a I'm-Determined-to-Own Account.

Cut your expenses. Hey, if you're saving for a downpayment, your focus should be on making money, not spending it. So all that money you were spending on entertainment and shopping can now go towards your downpayment account.

Get a second job. And now that you have all this extra time on your hands, you can use it to earn even more money.

Get a third job. Sell make-up. Hold sales parties. Walk dogs. House-sit. There are a million ways to make money. Employ as many of them as you can think of.

Does your insurance policy have a cash value against which you can borrow?

Take in a roommate and save what (s)he's paying you.

As for how to save for a downpayment, that's easy. If you want to save 20% as a downpayment (which you absotively, posolutely should), then take the amount you can afford to spend on a house, and divide it by 100 and multiply it by 20.
House value: $200,000
20%: $200,000 / 100 x 20 = $40,000
If you want to have that downpayment saved in five years, then you divide your downpayment goal by 60 (the number of months in 5 years) to come up with $666.66, which is how much you have to save every month. If that seems like too much, your options are to save for longer or to buy a less expensive home.

So, should you buy now or wait and save a bigger downpayment?

If you build up your downpayment, then you will end up paying less **interest**. You can avoid paying for mortgage **insurance**. And you reduce the **risk** of not being able to pay back the loan if the value of your home drops and you have to sell.

Of course, waiting has some cons too. First, you'll have to wait to own a home. You'll have to be disciplined or you could spend your savings on other stuff. And, of no small concern to some people, in some areas, house prices may rise faster than you can save the down payment.

My final thoughts on a downpayment: If you can't afford to save a downpayment - and by that I mean 20% down — what makes you think you'll be able to afford to maintain the home (rule of thumb: budget 3-5% of the value of your home for up-keep every year), pay your property taxes (yes, they will go up each year), and deal with the general challenges of home ownership. And if you're using a zero-down, low-interest mortgage to wedge yourself into a home, how will you cope with rates go up 1, 2, or 3%. Hey, rates will go up. (Yes, they'll go down too.) And how will you eat if your mortgage ends up costing you $300 a more a month when your cash flow is already tighter than a frog's ass?

Home ownership is great, if you do it right. Buy a home you can't afford, commit to payments that stress you out, and you'll rue it. Yup. Your home will be an albatross around your neck.

Remember, the point of life is to enjoy the moment. If all your moments are spent wondering when your house of cards will fall down, how much fun can you possibly be having?

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