



Understanding Buydowns



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Agenda

Buydown Defined

Permanent vs. Temporary Buydowns

GSE and MI Guidelines

Funding Buydowns

Borrower Considerations

Q/A

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What Is a Buydown?

A buydown is a mortgage financing technique with which the buyer attempts to obtain a lower interest rate for at least the first few years of the mortgage, or possibly its entire life.

Source: Investopedia

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Two Types of Buydowns

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Permanent Buydown

Temporary Buydown

Permanent Buydown

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A borrower may elect to pay points to PERMANENTLY buy down an interest rate

Buying the rate down by 0.25% will typically cost one full point of the loan amount as the buydown fee

Break-even point should be calculated



Example of Permanent Buydown

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- \$300,000 loan amount
- Borrower pays one point, or \$3,000, to buy down the rate by 0.25%
 - At 6.00%, the P&I payment would be \$1,798.66
 - At 5.75%, the P&I payment would be \$1,750.72
 - The savings would be \$47.94 per month
- The initial investment of \$3,000 is recovered in about 5 years
- Savings over the life of the 30-year loan would be \$17,257
- The buydown fee can be included in the allowable contributions



Temporary Buydown

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A borrower may elect a buydown fee that adjusts the payment for a TEMPORARY period of time at the beginning of the loan term

A one-time fee, known as a subsidy fee, applies

Common options include 3-2-1, 2-1 and 1-0

Example of 3-2-1 Buydown for Loan Amount of \$300,000



| Year | Interest Rate | Monthly P&I Payment | Monthly Savings | Annual Savings |
|--------|---------------|---------------------|-----------------|----------------|
| 1 | 4% | \$1,432.25 | \$563.66 | \$6,763.92 |
| 2 | 5% | \$1,610.46 | \$385.45 | \$4,625.40 |
| 3 | 6% | \$1,798.65 | \$197.26 | \$2,367.12 |
| 4 - 30 | 7% | \$1,995.91 | \$0 | \$0 |

Typically, the cost of the buydown is roughly equal to the amount the buyer would save in payment.

In this example, the total cost of the buydown (subsidy fee) is estimated to be \$13,756.

Example of 2-1 Buydown for Loan Amount of \$300,000



| Year | Interest Rate | Monthly P&I Payment | Monthly Savings | Annual Savings |
|--------|---------------|---------------------|-----------------|----------------|
| 1 | 5% | \$1,610.46 | \$385.45 | \$4,625.40 |
| 2 | 6% | \$1,798.65 | \$197.26 | \$2,367.12 |
| 3 - 30 | 7% | \$1,995.91 | \$0 | \$0 |

Typically, the cost of the buydown is roughly equal to the amount the buyer would save in payment.

In this example, the total cost of the buydown (subsidy fee) is estimated to be \$6,992.52.

Permanent vs. Temporary



- Using a sales price of \$300,000 and a loan amount of \$285,000
- Seller is willing to pay 3% contribution, or \$9,000

| Permanent Buydown (3% buys down rate by .75% to 6.25%) | P&I Payment | Loan Balance | Total Payments (cumulative) | Temporary 2-1 Buydown | P&I Payment | Loan Balance | Total Payments (cumulative) |
|---|-------------|--------------|--------------------------------|-----------------------|-------------|--------------|--------------------------------|
| Year 1 | \$1,754.79 | \$281,660.38 | \$ 21,057.60 | Year 1 = 5.0% | \$1,529.95 | \$282,104.84 | \$ 18,359.40 |
| Year 2 | \$1,754.79 | \$278,105.95 | \$ 42,115.20 | Year 2 = 6.0% | \$1,708.72 | \$279,000.39 | \$ 38,864.04 |
| Year 3 | \$1,754.79 | \$274,322.67 | \$ 63,172.80 | Year 3 = 7.0% | \$1,896.12 | \$275,671.53 | \$ 61,617.48 |
| Year 4 | \$1,754.79 | \$270,296.19 | \$ 84,230.40 | Year 4 = 7.0% | \$1,896.12 | \$272,101.97 | \$ 84,370.92 |

Total cost of 2-1 buydown is $\$4,394.04 + \$2,248.80 = \$6,642.84$
 Seller pays buydown plus additional \$2,357.16 toward closing

GSE Comparison Chart



| Agency | Allowed w/Fixed Rate | Allowed w/ARMs | Max Buydown Percentage | Max Rate Increase Per Year | Maximum Buydown Period | Exclusions | Interested Party Can Fund | Qualifying Rate |
|---|----------------------|----------------|------------------------|----------------------------|------------------------|--|---------------------------|---|
| Freddie Mac Selling Guide -4204.4 (10/1/21) | Yes * | Yes ** | 3% | 1% | 36 months | Investment C/O refinances Certain ARMs Manufactured | Yes *** | Note Rate or ARM Qualifying Rate |
| Fannie Mae Selling Guide -B2-1.4-04 (7/29/14) | Yes | Yes **** | 3% | 1% | 36 months | Investment C/O refinances Certain ARMs Manufactured | Yes | Note Rate or ARM Qualifying Rate |

*Temporary buydown permitted for Home Possible® secured by 1 to 2-unit properties

**ARM must have initial fixed rate for 5 years or more (7 years or more for 3 to 4 Unit primary residence)

***Lender credit derived from premium pricing cannot be used as credit toward funding buydown on a no cash-out refinance

****ARM must have initial fixed rate for 3 years or more

Note: Buydowns require a signed buydown agreement

What About MGIC Mortgage Insurance?



3.08.05 Interest Rate **Buydown** (Temporary or Permanent)

Follow MGIC Underwriting Summaries (3.02) and these guidelines:

- **Buydown** funds may be paid by the:
 - Borrower
 - Employer as part of an employee relocation benefit
 - Lender
 - Seller as part of the maximum allowable interested party contribution
- Maximum temporary **buydown**:

| Eligible Loan Types | Max. Annual Rate Increase | Property Unit Count | Max. LTV/CLTV | Buydown Schedule |
|---|---------------------------|---------------------|---------------|-------------------------|
| Fixed-rate, ARMs with ≥ 5 year initial fixed period, Balloons | 1% | 1 | 95% | 2% – 1% |
| | | | 90% | 3% – 2% – 1% |
| | | 2 | 95% | 2% – 1% |

- Qualification:
 - ARM with an initial term of 5 years – Use greater of note rate + 2% or FIAR
 - Fixed-rate or ARM with an initial term > 5 years – Use note rate
 - **Ineligible:** Cash-out refinance transactions, manufactured homes

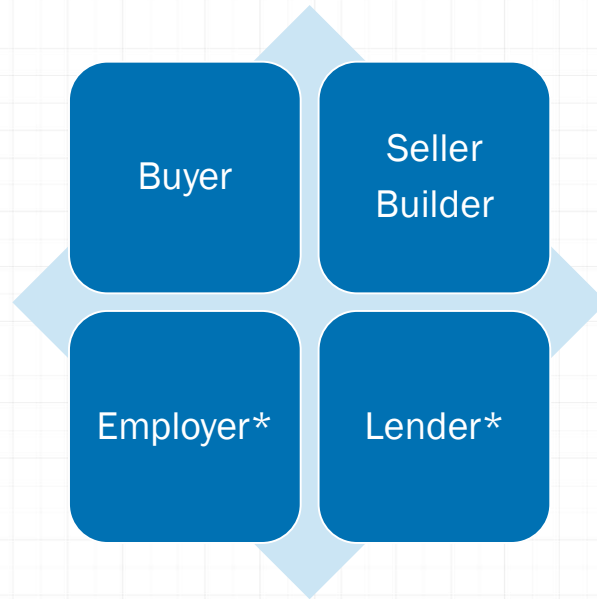
Source: MGIC Underwriting Guide – Standard Loans (9/22/22)

13



Who Can Buy Down a Rate?

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Interested-party contribution limits apply
* As allowed by internal guidelines

Pros and Cons of Buydowns










| Pros | Cons |
|--|--|
| <p>Temporary buydowns reduce the interest rate for short time, which results in a savings of money by lowering borrowers' mortgage payments during the initial term.</p> | <p>Once the temporary buydown rate ends, the increased monthly payment could result in payment shock.</p> |
| <p>A buydown may be a negotiation tool that allows you to pay less for the home than the seller's list price.</p> | <p>Buydowns may not be an option for certain loan types or property types.</p> |
| <p>A buydown is a good financing tactic for homebuyers whose income will increase in upcoming years.</p> | <p>If their income does not increase as expected, homeowners may struggle to make the mortgage payments.</p> |

15



Is a Buydown Right for Your Customer?

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-  How long do they plan to own the home?
-  Can interested-party contributions be negotiated?
-  Are they comfortable with the risk of their payment increasing?
-  Is it likely that their income will increase? Might it decrease?
-  Do they anticipate any major expenses – tuition, new car, remodeling?
-  What are their payment expectations?
-  Show them the options – run the numbers!



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Special Events



Special Event 60 minutes

Tackling Tough Topics – A Mortgage FAQ Session

November 14, 2022
2:30pm CST

[Register](#)

[View training details ▶](#)

Special Event 60 minutes

Speaking Confidently About Credit Reports With Your Borrowers

November 16, 2022
1:00pm CST

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Special Event 60 minutes

7x7 – 7 Videos LOs Should Be Doing Today and 7 Ways to Implement Them

November 21, 2022
2:00pm CST

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