



RED OAK
MORTGAGE, INC
NMLS 5415

Breaking Down Buydowns

December 2022



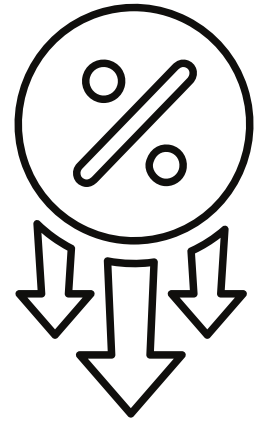
The Lineup

- What is a Buydown?
- Temporary Buydown
- Permanent Buydown
- Temporary vs Permanent
- Who Can Buydown a Rate?
- Buydown Pros & Cons
- Buydown for the Consumer



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.



Types of Buydowns

- Temporary Buydown
- Permanent Buydown

Source: Investopedia



Temporary Buydown

The Process

- 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
 - 1-0



Temporary Buydown

Example of a 3-2-1 Buydown

Loan Amount: \$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	\$0.00	\$0.00

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.



Temporary Buydown

Example of a 2-1 Buydown

Loan Amount: \$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	\$0.00	\$0.00

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 Buydown

The Process

- A borrower may elect to pay points to **PERMANENTLY** buydown 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 to ensure optimal benefit



Permanent Buydown

Example

- Loan Amount: \$300,000
- Borrower pays one point, or \$3,000, to buydown 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 vs Permanent

- 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*	P&I PAYMENT	LOAN BALANCE	TOTAL PAYMENTS (CUMULATIVE)
Year 1	\$1,754.79	\$281,660.38	\$21,057.60
Year 2	\$1,754.79	\$278,105.95	\$42,115.20
Year 3	\$1,754.79	\$274,322.67	\$63,172.80
Year 4	\$1,754.79	\$270,296.19	\$84,230.40

*3% buys down rate by 0.75% to 6.25%

TEMPORARY 2-1 BUYDOWN	P&I PAYMENT	LOAN BALANCE	TOTAL PAYMENTS (CUMULATIVE)
Year 1 = 5.0%	\$1,529.95	\$282,104.84	\$18,359.40
Year 2 = 6.0%	\$1,708.72	\$279,000.39	\$38,864.04
Year 3 = 7.0%	\$1,896.12	\$275,671.53	\$61,617.48
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



Who Can Buydown a Rate?

Buyer



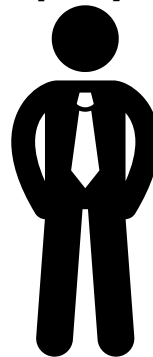
Seller



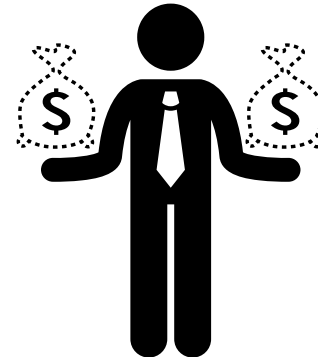
Builder



Employer*



Lender*



* As allowed by internal guidelines

Interested-party contribution limits apply



Buydown Pros & Cons

PROS

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.

A buydown may be a negotiation tool that allows you to pay less for the home than the seller's list price.

A buydown is a good financing tactic for homebuyers whose income will increase in upcoming years.

CONS

Once the temporary buydown rate ends, the increased monthly payment could result in payment shock.

Buydowns may not be an option for certain loan types or property types.

If their income does not increase as expected, homeowners may struggle to make the mortgage payments.



Buydown for the Consumer


Is a buydown right for me?

Depends on the following:

- How long do I plan to own the home?
- Can seller concessions be negotiated?
- Am I comfortable with the risk of the payment increasing?
- Is it likely that my income will increase? Might it decrease?
- Do I anticipate any major expenses - tuition, new car, remodeling?
- What are my payment expectations?
- What are my options? Need to run the numbers with my Loan Officer!



**Interested?
Contact us for
more information at:**

 732-410-4141

 info@redoakmortgage.com

 redoakmortgage.com/buydowns

We look forward to helping you achieve your homeownership goals!

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