

## Capital One: How to Calculate Your Debt-to-Income Ratio

**With this simple formula, you can get a better idea of how much house you might be able to afford.**

You want to buy a home, but how easily will you be able to manage a mortgage payment, along with taking care of your other debts? You can expect your lender to be asking the same question.

One of the ways that loan officers determine how much mortgage you can afford is by calculating your debt-to-income ratio, or DTI. It's a simple formula, and it's something you can use to help you set a realistic budget.

### **What's Included and What Isn't**

To find your DTI, simply add up all your monthly debt payments and divide the amount by your gross monthly income—the total amount of money you make each month before taxes. That'll show you what percentage of your income is going toward paying off debt.

Let's look at an example of how this works. Suppose that each month you have income of \$5,000, before taxes, and your debt payments are \$1,000. Now, divide \$1,000 by \$5,000, which equals 0.20. But because DTI is a percentage, you have one more step. Take the answer, in this case 0.20, multiply it by 100, and you've got your DTI—20 percent.

*“Don't be surprised if lenders want you to have a DTI of no more than 43 percent. However, if yours is higher, there are ways you can lower your ratio.”*

When you're totaling your debt, be sure you don't include things like utility bills and food that can change from month to month. Your debt in the DTI calculation means the regular payments you're required to make, such as student loans, alimony, car loans, minimum credit card payments, and other similar items.

Every lender is different, but they may want you to have a DTI of no more than 43 percent, including your new mortgage payment. Many times, that's going to be viewed as the maximum debt ratio that would let you make a monthly mortgage payment without it causing too much stress on your budget (1). With our example of \$5,000 in pretax income and \$1,000 of debt, you would be at a 43 percent DTI with a monthly mortgage payment of \$1,150. When you're looking around on the Internet, you may find some lenders who want to see a lower number, maybe a 36 percent maximum DTI. Still others might say they'll go higher.

Breaking out only the home loan portion of your total DTI, lenders generally seem to want it to be no more than 28 percent of your pretax income.

### **Improving Your Ratio**

Ideally, the lower your DTI is, the better. But if it is on the higher side, don't panic. Talk to a mortgage lender about your options, and start making a plan for paying off a chunk your debt. If you can, try to get your debt as low as possible before you apply for a mortgage. And even though it's not necessarily easy to do, another way to lower your DTI is to increase your monthly gross income, if possible.

As with most home loan questions, you'll be helping yourself by finding a professional. They can look at your specific situation and help you go from there.

(1)Consumer Financial Protection Bureau: What the new CFPB mortgage rules mean for families and homeowners

– [http://files.consumerfinance.gov/f/201312\\_cfpb\\_mortgagerules.pdf](http://files.consumerfinance.gov/f/201312_cfpb_mortgagerules.pdf)

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