

## Spring E-Newsletter (PART II): Comparing Mexico and U.S. Mortgages - How Different are Rates, Costs and Programs?

Written by Matthew A. Miller and Tina Rebello, ConfiCasa Mortgage International

### INTRODUCTION

Here we will answer the most common question asked “**Why are rates higher in Mexico?**” In order to answer this question, we thought it best to provide a **direct comparison** between a second home mortgage in the U.S. and that in Mexico to show you that **rates are closer than you think . . . .**

#### U.S. Second Home Mortgage

Purchase Price of \$650,000

Minimum Down Payment = 20%

Minimum Starting Rate on Jumbo = 6.0%

Hit for Self-Employed Borrower = +0.75%

Hit for FICO less than 700 = +0.5%

**Rate starts at 7.25%**

#### Mexico Second Home Mortgage

Purchase Price of \$650,000

Minimum Down Payment = 20%

Must prove qualifications

Must have FICO greater than 650 - 680

No hit for FICO less than 700

**Rate starts at 7.75%**

### THE MISCONCEPTIONS

**Rates are Closer Than You Think.** Rate differences (as shown above) between the two types of mortgages have decreased significantly as Mexico second home mortgages have decreased while U.S. second home mortgages have increased. Further, U.S. second home mortgages have always been more expensive than primary residences.

**Comparing Apples to Apples.** A common mistake is comparing Mexico second home mortgages with U.S. primary mortgages. While we understand that American buyers are used to very low U.S. primary mortgages, rates for a second home mortgage are of course higher and often not well-understood.

**U.S. Mortgage Programs Have Become Less Affordable.** U.S. homeowners have become accustomed to easy to obtain, no money down, low interest (often interest only) mortgages. Unfortunately, this has led to the real estate/mortgage market meltdown in the U.S. making the U.S. mortgage not as affordable as it once was. Moreover, U.S. homeowners have used equity lines of credit to purchase second homes which are now extremely difficult to obtain.

**Costs are More Competitive Than They Appear.** Because Mexico second home mortgages are held by the banks that underwrite the loans (as compared to U.S. second home mortgages which are sold in the secondary market), costs associated with the two programs are structured very

differently. Mexico second home mortgages charge fees on the front on through loan origination points. U.S. first and second home mortgages sometimes charge upfront points but more likely charge their fees as part of the interest rate (known as “yield spread premium” or “YSP”). Therefore, it is more difficult to see the true costs of a U.S. second home mortgage, but often they are equal or often even greater than that of a Mexico mortgage. Again, the main difference of the two is that a borrower pays the full cost of the loan at closing (for a Mexico mortgage) as compared to spreading the costs over the life of the loan through higher interest payments (for a U.S. mortgage).

**Loan Programs are Difficult to Compare.** Overall, it is difficult to compare a second home mortgage in the U.S. and in Mexico as they are very differently structured loan programs. It is therefore best to better understand the differences.

**Loan Amounts** - Larger loan amounts have become extremely difficult to obtain for U.S. second home mortgages while larger loan amounts (from \$1,000,000 to \$5,000,000) fit within normal guidelines in Mexico.

**Volatility/Uncertainty** - Given the secondary market structure of U.S. mortgages, rates, guidelines, and costs change every day, whereas Mexico mortgages only change semi-annually or annually providing more assurance on loan commitments.

**Loan Program Guidelines** - Given the U.S. real estate turmoil, U.S. second home mortgages can be complex in understanding qualifications and rates while Mexico second home mortgages have been tailored.

**Problem markets** - There are many U.S. second home/vacation markets which are experiencing price depreciation. As a result, second home mortgages are becoming spottier and harder to obtain. For the most part, Mexico is not currently experiencing the same market turmoil and thus very few trouble areas exist.

## **BOTTOM LINE:**

**Second home mortgages (whether for a U.S. property or Mexico property) are going to be more expensive than a U.S. first home mortgage. The reason is two-fold.**

First, lenders offering cross-border Mexico home financing programs are U.S. and international finance institutions, lending in a foreign country. While we (and you) already know that Mexico’s resort markets are a safe place and have huge potential as they continue to become the premier destination for second homes and retirees throughout North America, they are still different than the U.S. or Canada. Therefore, some country risk does exist for lenders as does the risk of “resort destinations”.

Second and more importantly, the financial institutions that underwrite Mexico mortgage loans

hold onto the loans as opposed to packaging them and selling them in the secondary market (think the U.S. mortgage market a couple of decades ago). Further, government created agencies who purchase and guarantee such mortgages (as done in the U.S. through Fannie Mae, Freddie Mac or the FHA) do not exist for Mexico mortgages. If you have somewhat followed the recent U.S. housing crisis you may have learned that packaging and selling loans in the secondary market drives rates and down payments lower as this method was supposed to decrease risk to the ultimate note holder. But, as you also may know, this really didn't spread risk but created risk that was not at all understood, thus resulting in the housing market landslide that we are seeing today. So while down payments and interest rates may be higher for foreigners buying Mexico real estate as compared to the U.S., there is certainly upside to all of this. The upside is a decreased likeliness for Mexico mortgages to create the problems seen recently in the U.S. real estate market.

Second homes are considered riskier in the eyes of a lender given the nature of their use. **When you break it all down and fully understand the differences, the fact that interest rates for Mexico second homes are often in line with U.S. second homes, financing a Mexico home looks far more attractive than first thought.**