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ROB CARRICK

Can you really afford that mortgage? Know your Real Life Ratio

ROB CARRICK

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Someone ought to explain the facts of life to the nation's bankers.

They're handing out mortgages to people without any apparent understanding that today's home-buying couple is tomorrow's family of three or four. A lot happens to one's ability to afford mortgage payments when kids come along, but you'd never know it by the way lenders qualify borrowers.

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Never take a lender's word for it that you can afford a house. Instead, try a new tool I've created called the Real Life Ratio.

Download the Real Life Ratio interactive spreadsheet [here](#).

It's designed to show how well you'll be able to handle the basic monthly costs of home ownership, plus real life expenses such as cars, daycare and long-term home maintenance. Prospective home buyers should try it, and so should existing homeowners who want to see how well they're handling their finances.

The Real Life Ratio is an expansion of a simple affordability measure [I introduced last year called the Total Debt Service and Savings Ratio](#), or TDSS. The idea of creating something more comprehensive came to me after [a Globe and Mail series on daycare](#) was published last fall. We heard from many people about how hard it was to manage the cost of a mortgage in today's expensive housing market, on top of daycare and other costs.

Use the Real Life Ratio and you'll know what you're getting into before you buy a house. You may decide you need to save a bigger down payment, buy a smaller house, live in a cheaper location or not buy at all.

Here are a few important things to know about the ratio:

1. Household take-home pay is used here: Other ratios use gross income, which is less relevant for practical financial planning.
2. This is not a budget: Only fixed costs are included here; food, clothing and other costs aren't discretionary, but you decide how much to spend.
3. Costs for home maintenance and improvement are included: You won't face these costs every year, but on a long-term basis they might average about 1 per cent of your home's value annually; maybe less for brand new homes and more for older ones.
4. There's a slot to include condo fees: Be sure to add any monthly utility costs that are not included in your condo fees.
5. Your local real estate market plays a big role: A liveable Real Life Ratio may be harder to achieve in big cities with roaring real estate markets.

Guidelines on how to interpret the ratio are provided. For optimum results, make a list of your monthly spending on food, transportation, entertainment and everything else not included in the ratio. Then, see

whether your lifestyle is affordable. If your Real Life Ratio is 80, could you get by on 20 per cent of your take-home pay?

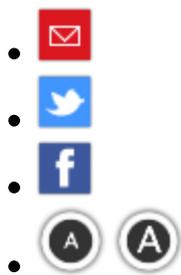
Keep in mind that your ratio will change – for the worse if you have kids in daycare and have a couple of cars, and for the better once your kids are out of daycare and you move into your prime earning years.

To ensure the Real Life Ratio reflects real life, I consulted four financial planners. Thanks to Rona Birenbaum, Barbara Garbens, Kurt Rosentreter and Renée Verret for some useful suggestions based in part on spending patterns of their own clients.

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