American Journal of
Biomedical Science & Research

www.biomedgrid.com
ISSN: 2642-1747

Short Communication

An Assumable Mortgage Maybe the Solution

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***To Cite This article:** David Dai, Caleb Dai and Dongfeng Wu*, An Assumable Mortgage Maybe the Solution. Am J Biomed Sci & Res. 2025 29(4) AJBSR.MS.ID.003814,* **DOI:** 10.34297/AJBSR.2025.29.003814

Received: December 05, 2024; **Published:** December 15, 2025

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There have been numerous news reports on the crisis in the real estate market recently. We are all aware that the real estate market has been stagnant for some time. The problem is a combination of high house prices, high mortgage rates, and economic uncertainty. How to solve the current crisis is very important to the US economy. Basically, the high prices and high mortgage rates have made it almost impossible for first-time home buyers to enter the market. As a possible solution, President Trump and the US Government are considering a 50-year fixed-rate mortgage to stimulate the housing market, and Fannie Mae has even eliminated its minimum 620 credit score requirement for borrowers seeking loans [1]. While a 50-year mortgage can lower the monthly payment, it could deprive buyers in the long term: it is hard to build up home equity. And for those who buy their houses using the 50-year loan in their 30s, they are most likely still paying a mortgage in their 80s. Therefore, this may not be the right way to handle the current housing crisis. On the other hand, removing the minimum credit score may help a little, but it may incur high risk, such as the subprime crisis from 2008 to 2009.

The main problem is that there are not enough buyers due to the high mortgage rate. There are millions of younger generations in their thirties who want to buy a house, but due to the current high mortgage rate, they are sitting on the fence and wish the mortgage rate could be lower in a few years. The current 30-year fixed mortgage is right above 6%, which is normal according to the historical data; however, it is much higher than the 3 or 4% that was secured by most homeowners before or during the pandemic. So, there is little motivation for most homeowners to sell as well. Because if they sell, it is hard to get a loan at a low rate to buy a similar house. The historically low rate in those years has dramatically inflated the house prices, making it more difficult for potential buyers, especially first-time house buyers, as their income has not increased at the same rate as the housing prices. Even though the Federal Bank lowered the overnight interest rate, the mortgage rate that is tied to the 10-year bonds doesn't necessarily follow suit. Therefore, this is the current dilemma of the housing market: a low rate in the past has inflated the house price, and now the normal rate (it surely is higher than before) makes it unreachable for younger generations to buy. So, helping home buyers secure a comparatively lower mortgage interest rate as a transition is critical right now.

We think that an assumable loan could be a possible solution to achieve this. So, what is an assumable loan? By definition, an assumable loan means a homeowner (the seller) agrees to transfer the outstanding mortgage on their home to the buyer when their home has been purchased [2]. This is especially helpful if the seller has a low fixed-rate mortgage, such as a 30-year loan at 3%, and has not been in the house for too long. Let's use a concrete example to illustrate how to carry out an assumable loan. Suppose a homeowner bought his home at the price of $330K in 2020, which was close to the national median price of $329K in the US at that time, and he secured a 30-year mortgage at a fixed rate of 3%. He paid 5% down payment (i.e., $330K *0.05=$16.5K), and he took out a loan at the amount of $330K*0.95=$313.5K. Using the loan calculator [3], his monthly payment of interest and principal would be $1321.73 (not including insurance and property tax). And at the end of the fifth year (such as now in 2025), he would have accumulated some home equity, and the principal balance would be $278,721.45. Now, if he sold his house at the national median of $415K in 2025, the buyer who wants to use the assumable loan can take over the principal balance of $278,721.45, at the fixed rate of 3%. But the buyer must pay the difference between the total price of $415K and $278,721.45, which is close to $136.2K. Since most buyers cannot afford so much cash, they need to take out a second loan, assuming that it is a 30-year fixed rate of 6% for the loan amount of $120K, if the buyer paid a down payment of $16.2K. Using the loan calculator, his monthly payment of interest and principal for the second loan would be $719.46. Adding the two loans together, the buyer would need to pay $1321.73+$719.46=$2041.19 per month to cover the interest and the principal. Compared with a regular 30-year mortgage of the amount of $398.8K (i.e., the total price $415K minus his down payment of $16.2K, so his loan amount is $398.8K) at 6%, the buyer would have to pay $2391.01 per month to cover the interest and the principal [3]. Therefore, the buyer could have saved $2391.01-2041.19=$349.82 per month. It is recommended that the housing payment should be limited to 1/3 of one's gross monthly income. Since the above calculation has not included the home insurance and property tax, let's assume that the principal and interest payment should be limited to one-quarter of one's monthly income. Using the assumable mortgage, the buyer should have a gross monthly income of $2041.19*4=$8164.76, or an annual gross income of $97,977. Without the assumable mortgage, the buyers would have to make $2391.01*4=$9564 per month, or $114,768 annually. So, even though the difference in the monthly payment is small, there is a huge difference in the annual income requirement.

One possible problem with assumable loans is loan default. So, it is necessary to require that the 2nd mortgage be taken from the same bank as the assumable loan. It could be a win-win-win situation for the three parties if it is carried out correctly: The seller can sell more easily with this loan arrangement; the buyers can afford the home with a lower monthly payment; the bank issues a second loan to the buyer and makes more money as well. Hopefully, this will break down the vicious cycle of the current housing problem and bring back a healthy, prosperous housing market in the long run. Currently, there are three large agencies that offer assumable loans: Federal Housing Administration (FHA) [3], United States Department of Agriculture (USDA) [4], and U.S. Department of Veterans Affairs (VA) [5]. Potential buyers can surf their websites and find more information [6].

Finally, we want to point out that this arrangement should be transitional, which means the assumable mortgage should be allowed only for the original loan borrower, and the buyer who used the assumable loan cannot transfer it to the next buyer in the future, so that the assumable loan should be phased out in the next couple of years. The reason is that an extremely low mortgage rate is not good for the housing market in the long run, as it will inflate housing prices dramatically, making it difficult for first-time buyers. This is the same reason that a low (or close to zero) interest rate for a savings account is a robbery of the middle class in general. Most middle-class families cannot gain anything by putting their money in a bank in a low-interest environment, and they are forced to put their money in the stock market, where they will most likely lose the money.

In summary, the assumable loan is a transitional arrangement to help relieve the current crisis. Eventually, the housing market will have to adjust to the normal long-term rate, which is between 5% and 7% for a 30-year mortgage if the annual inflation rate is capped at 3%. This should be the goal of a healthy housing market for the long term.

Acknowledgement

None.

Conflict of Interest

None.

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