3 steps to calculate your debt-to-income ratio

Written by Dori Zinn, Edited by Pippin Wilbers

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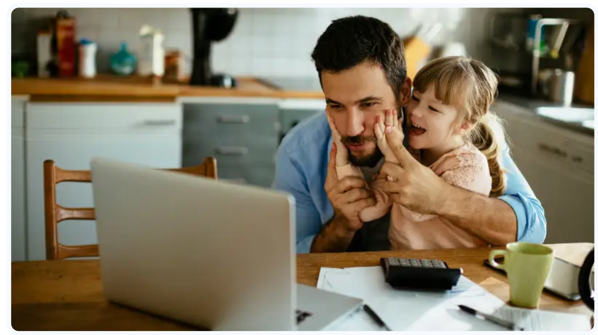

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Key takeaways

- To calculate your debt-to-income ratio, add up your monthly debt payments and your gross monthly income and then divide your debt by your gross income.
- While every lender and product will have different ranges, a DTI nearing 50 percent is considered high by most companies.
- Your DTI greatly impacts your ability to get approved for a loan or mortgage.

Your debt-to-income ratio (DTI) is your total monthly debt payments divided by your total gross monthly income. You can calculate it by following a few simple steps. It helps lenders determine your approval odds and the likelihood of you being able to make your monthly payments.

The higher your DTI, the more debt you have compared to your income, which signals to lenders that you may struggle to cover debts and other expenses. The lower your DTI, the more lenders see you as a reliable borrower.

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Step one: Add up your

monthly debts

Start by adding up all your debts listed on your credit report, including:

- Auto loan payments.
- Child support and alimony payments.
- Credit card payments.
- Home equity loan payments.
- Home equity line of credit payments.
- Line of credit payments.
- Mortgage payments.
- Personal loan payments.
- Store card payments.
- Student loan payments.
- Timeshare payments.

In addition to your personal debts, you should also include any joint accounts or co-signed loans.

Use your monthly payment for fixed-rate loans like personal loans and auto loans. Use your minimum monthly payment for variable-rate accounts like credit cards and home equity lines of credit.

For your mortgage, calculate the full PITI — principal, interest, taxes and insurance. This will be your regular monthly payment if you escrow your taxes and insurance. If you don't escrow, your lender will likely take your annual tax and insurance payments, divide them by 12 and include them as part of your mortgage payment for purposes of your DTI calculation.

Here is an example of what it could look like after considering these monthly debts:

- Mortgage: $1,600
- Auto loan: $300
- Minimum credit card payments: $300
- Student loan: $200

Total monthly debts: $2,400

Learn more: **Try Bankrate's personal loan calculator**

Step two: Add up your monthly gross income

Next, add up your monthly gross income. This should include wages from any traditional jobs as well as any gig or freelance work you do. However, you do not need to include payments like alimony or child support unless you want that to be considered by the lender.

If you are a W-2 employee, documentation will likely come from your W-2 form or your last several pay stubs. If you are self-employed or have income from a side hustle, your lender will likely look at your business tax returns and 1099 forms.

If you have money coming in from a side hustle but don't have a business tax return or other documentation, your lender may not allow you to use that income as part of your DTI calculation. However, some may allow bank statements that show regular deposits.

If you have properties you rent out, you need to include them in your income as well. The mortgage payments on your rental properties are included as part of your monthly debts.

However, you may not be able to use all of the rental income as part of your income calculation. Many lenders will only allow you to count 75 percent of the monthly rent towards income. That leaves a buffer for maintenance and vacancies.

Here is how those calculations could go:

- Monthly gross income from day job: $5,000
- Side hustle monthly gross income: $1,000

Total monthly gross income: $6,000

Step three: Divide your monthly debts by your monthly gross income

For this example, divide your monthly debt payments ($2,400) by your total monthly gross income ($6,000). In this case, your total DTI would be 0.40, or 40 percent. To confirm your number, use a DTI calculator.

Understanding your debt-to-income ratio

The higher your DTI, the riskier you appear to lenders. Each lender has different DTI standards you must meet to qualify for a loan. Here's a closer look at what these percentages mean:

- **Under 36 percent:** Most lenders see DTIs in this range as ideal, and you shouldn't face challenges getting approved for funding assuming you meet the other lending guidelines.
- **36 percent to 41 percent:** You could get approved with a DTI in this range, but the lender could request that you lower it if you're seeking a large loan amount.
- **42 percent to 50 percent:** Your debt load is on the higher end in relation to your income. The lender may be hesitant to extend funding to you, as an additional debt payment could stretch your budget too thin.
- **Over 50 percent:** It could be challenging to get approved by most lenders.

Keep in mind that the requirements differ for each lender and the type of loan you take out so read the minimum requirements and eligibility criteria carefully before applying. For example, the lender's maximum DTI for a mortgage might not be the same as its maximum DTI for a personal loan, so research the lender's eligibility distinctions and where your DTI lands.

The bottom line

Lenders take your DTI very seriously. It's one of the primary approval considerations for a loan. If your DTI is above 50 percent, it may be harder to get approved for additional credit, so do your best to lower your DTI before taking on any new debt if possible.

Frequently asked questions

What should you do once you know your debt-to-income ratio?

Do current lenders need to know if your debt-to-income ratio changes?

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Written by

Dori Zinn

Contributor, Personal Finance

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Dori Zinn has been a personal finance journalist for more than a decade. Aside from her work for Bankrate, her bylines have appeared on CNET, Yahoo Finance, MSN Money, Wirecutter, Quartz, Inc. and more. She loves helping people learn about money, specializing in topics like investing, real estate, borrowing money and financial literacy.

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