Your dream home becomes a nightmare...

...when you end up "house poor" with most of your money going to pay for the mortgage and little left over for enjoyment.

When buying a home, you need to be practical and realistic. Over-extending yourself financially is the quickest way to destroy the excitement of owning your own home. A real estate professional can help you find the home of your dreams; a realtor can also assist you in evaluating mortgage options and obtaining financing at the most attractive prevailing rate. In the meantime, here are some ways to determine your "affordability quotient."

Setting a maximum price range is more important than simply establishing an upper price limit because unanticipated costs could push you into the "house poor" danger zone. To determine your affordability price range, you must calculate two amounts, the amount of cash you can afford to put towards the purchase (the down payment) and the maximum amount of loan (mortgage) you can comfortably carry.

A mortgage covers the difference between the purchase price and your down payment. The larger the down payment, the less you have to borrow, the smaller your monthly mortgage payment and the lower your cost of interest over the term of the mortgage. So it probably makes sense to put down as much of your own money as possible.

You should keep a cash reserve for unexpected expenses and such typical "post purchase" expenses as land transfer tax, legal fees, mortgage arrangements, moving expenses, new furnishings and appliances.

The first step towards establishing a maximum mortgage limit is to calculate a monthly payment you can afford. Financial institutions do this by calculating your debt-service ratio.

To calculate your debt-service ratio, list all your loans (car, personal loans, monthly credit card balances). The sum of these loan payments and your mortgage payment (including principal, interest and taxes) should not exceed approximately 40 per cent of your gross income. The mortgage payment and taxes should not exceed approximately 30 per cent of your gross income.

The size of the mortgage you can arrange, based on payments you can afford, depends on interest rates. The lower the rates, the larger the possible mortgage and the more affordable the housing is.

But there are other mortgage terms to consider as well. How open is the mortgage? Would prepayment be allowed? Is the mortgage affordable?

Discuss your mortgage options with a realtor, your banker or a financial advisor. Establish a limit and stick to it.

The usual source of mortgage funds is a lending institution that determines the maximum loan allowed. But there are other sources of funding, too and a realtor can help you choose the best lender at the best rate and terms.