

# Financing Methods

## Fixed-Rate Mortgage

The interest rate stays the same for the entire term of the loan - usually 15 or 30 years, so the interest and principal portions of your monthly payment remain the same. Your payments are stable and predictable, but initial interest rates tend to be higher on a fixed-rate mortgage than on adjustable-rate loans.

## Adjustable-Rate Mortgage (ARM)

The interest on an adjustable-rate mortgage is linked to a financial index, such as a Treasury security, so your monthly payments can vary, up or down, over the life of the loan - usually 30 years. Some adjustable-rate mortgages have a cap on the interest rate increase to protect the borrower.

The lower initial payments on ARMs make it easier for buyers to qualify.

## Adjustable-Rate Mortgage Terms

- **Adjustment Period:** The length of time between interest rate changes on an ARM. For example, a loan with an adjustment period of one year is called a one-year ARM, which means that the interest rate can change once a year.
- **Annual Percentage Rate (APR):** The total finance charge (interest, loan fees, points) expressed as a percentage of the loan amount.
- **Cap:** The limit on how much an interest rate or monthly payment can change, either at each adjustment or over the life of the mortgage.
- **Conversion Clause:** A provision in some ARMs that enables you to change an ARM to a fixed-rate loan, usually after the first adjustment period. The new fixed rate is generally set at the prevailing interest rate for fixed-rate mortgages. This conversion feature may cost extra.
- **Index:** A measure of interest rate changes used to determine changes in an ARM's interest rate over the term of the loan.
- **Margin:** The number of percentage points a lender adds to the index rate to calculate the ARM interest rate at each adjustment.

