

30-Year Fixed, Interest Only *an introduction*

The lending community is always dreaming up new and innovative loan programs but most offer few benefits over those programs already being offered. Two recent examples are the 40-year and 50-year mortgages, both of which act more as marketing gimmicks than feasible loan products. Sadly, the strategy works and many homeowners chase these new products in search of untapped payment relief.

Every now and then, a new product is introduced that provides real benefits for homeowners. The 30-year fixed mortgage with an initial 10-year interest only option is such a product, particularly in an increasing interest rate environment like the one we've been in since mid-2003. If you've heard of these loans or if you're curious to know more, here are a few thoughts for you to consider.

The obvious allure of interest-only options is their ability to lower your monthly payment. There are actually three options: amortized payments, interest only payments and negative amortization payments. Amortized payments require both principle AND interest in each payment. Interest only payments imply no principle repayment, reducing your payment. Negative amortization payments allow borrowers to make payments that are not even enough to pay the interest, resulting in even lower payments along with a rising mortgage balance.

While amortized payments are the most conservative and contribute to the repayment of the original loan balance, interest only payments are lower and you can always add more to your individual payments when your budget allows. These small additions all get allocated directly to the principle balance so you can achieve the same end result while maintaining more flexibility along the way.

Negative amortization programs, like Option ARMs, are dangerous and I caution clients against them whenever possible. Yes, they can dramatically lower your monthly payments (good for investors) but they erode your equity and they're also based on a variable interest rate, subjecting you to additional market risks.

The new 30-year fixed mortgage with a 10-year interest only option gives you a fixed rate for the full 30 years. Nothing can change the interest rate. It's completely fixed. But for the first 10 years, you're only required to pay the interest. If you want to pay more, you can but it's not required. On the 10-year anniversary, the payments are recalculated to ensure the full repayment of the loan within the remaining 20 years. That means your monthly payment will increase at that time but the rate never changes, allowing you to possibly avoid refinancing.

Of all the transactions I've done so far in 2006, many have included this loan product. The interest rate differential between this product and a similar product that's only fixed for 5 or 7 years is very small so the premium you're paying for a fixed interest rate is much smaller than it was just two years ago. Please give me a call if you have questions about this product. With interest rates on the rise, it's a great time to consider permanently locking your rate, particularly if you plan to stay in your current house for a number of years yet to come.