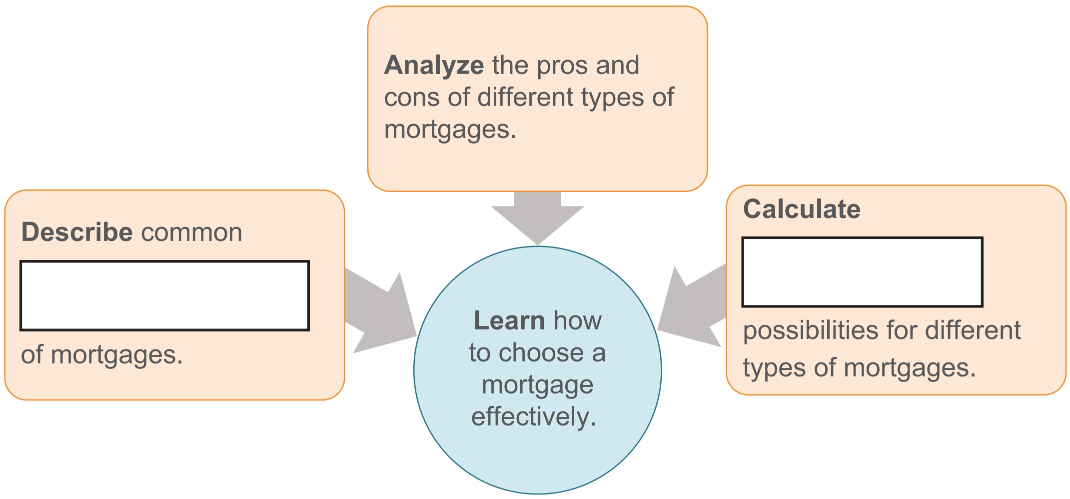
Warm-Up | Mortgages and Home Ownership

Lesson Question

Lesson Goals



Words to Know

Fill in this table as you work through the lesson. You may also use the glossary to help you.

	the level of trustworthiness of a borrower
	an event or outcome that happens as a result of previous decisions and actions
	the amount of money initially borrowed as part of a loan
	a legal agreement that determines repayment for a loan used to buy a home or other property

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Mortgages

A **mortgage** is a [ ] agreement between a person and a bank.

- A borrower agrees to a loan amount, an [ ], and a payment term.
- The borrower pays the [ ] back over time, usually over many years.

Mortgages are necessary for most people.

Budgeting for Larger Expenses

[ ]:

- can last for up to 30 years or more.
- should make up no more than 20–25% of a budget.

Mortgages involve careful planning.

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Principal

In a mortgage, the **principal** is the amount of money initially ______ from the lender.

This can include:

- the full price of the house.
- additional ______.

Sample Mortgage

Home price: $300,000

Repayment terms: 30 years

Principal: $300,000

Down Payments

A down payment is required for most mortgages.

- The down payment amount is determined by the ______ of loan and your credit score.
- Down payments range from ______% of the price of the home.

Sample Mortgage

Home price: $300,000

Down payment percent: 20%

Down payment: $60,000

Fees

A mortgage often involves additional fees.

- Fees charged by the ______ for processing the loan
- ______ paid to state or local governments

Components	Cost
Principal after down payment	$240,000
Origination fee	$1,200
Closing costs	$4,800
Total principal	**$246,000**
Additional taxes	**$4,000**

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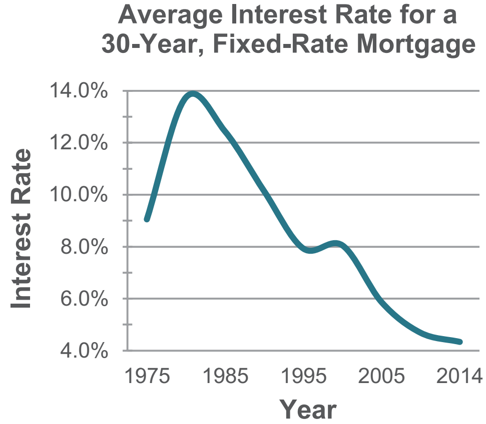
Interest Rates

The interest rate is the [ ] of borrowing money and is listed as a percentage.

- Average rates [ ] as a consequence of changes in the market.
- Lenders review a borrower's [ ] when choosing an interest rate to offer.

Circle the interest rate at which it was really bad time to buy a house.



Points

A point is a [ ] fee that a borrower can pay to [ ] the interest rate.

- The cost of a point often equals [ ] percent of the loan amount.
- Points can lower the interest rate in varying amounts.

	Number of points		
	0	**1**	**2**
Borrower cost	$0	$2,400	$4,800
Interest rate	5.0%	4.0%	3.0%

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Monthly Payments

There are many factors that can affect your monthly payment.

- Down payment
- ________
- Loan amount
- Loan ________

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Types of Mortgages

Mortgages are commonly set up in three different ways.

Types of mortgages

- ________ rate
- ________ rate
- Balloon payment

Fixed Rate Mortgages

A fixed-rate mortgage is the ________ type of mortgage.

- The interest rate stays ________ through the life of the loan.
- The outside economy does not affect the interest rate or monthly payments.

Sample Mortgage

Interest in year 1: 4.5%

Interest in year 15: 4.5%

Interest in year 30: 4.5%

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Calculating a Fixed-Rate Mortgage Payment

Components	Cost
(P) Principal	$200,000
(R) Monthly interest rate	.4%
(n) Total number of monthly payments (30-year term)	360
(M) Monthly payment	

Circle the principal in the formula.

Formula for monthly payment:

$$M = P\frac{[R(1+R)^n]}{[(1+R)^n - 1]}$$

Calculating a Fixed-Rate Mortgage Payment

Component	Cost
(P) Principal	$200,000
(R) Monthly interest rate	.4%
(n) Total number of monthly payments (30-year term)	360
(M) Monthly payment	

Circle the principal in the formula.

Formula for monthly payment:

$$M = 200{,}000\frac{[.004(1.004)^{360}]}{[(1.004)^{360} - 1]}$$

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Calculating a Fixed-Rate Mortgage Payment

Component	Cost
(P) Principal	$200,000
(R) Monthly interest rate	.4%
(n) Total number of monthly payments (30-year term)	360
(M) Monthly payment	

Formula for monthly payment:

$$M = 200{,}000\frac{[.017]}{[3.208]}$$

Fixed-Rate Mortgages: Pros and Cons

Pros

- The interest rate stays the ______ over the entire term.
- Monthly payments are ______.
- If interest rates rise on the market, a borrower could benefit by keeping a lower rate.

Cons

- If interest rates ______ on the market, a borrower could be stuck paying a ______ rate.

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Adjustable-Rate Mortgages

An adjustable-rate mortgage (ARM) is another common type of mortgage.

- The interest rate can ________ on a yearly basis.
- Changes are often tied to Federal Reserve interest rates.
- The amount a rate can change is usually ________.

Sample Mortgage

Interest in year 1: 4.5%

Interest in year 15: 5.2%

Interest in year 30: 6.9%

The Effect of Adjustments

Before adjustment

Component	Cost
(P) Principal	$200,000
(R) Monthly interest rate	.4%
(n) Total number of monthly payments remaining	360
(M) Monthly payment	**$1,059.85**

The annual interest rate is ________%.

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The Effect of Adjustments

Before adjustment

Component	Cost
(P) Principal	$200,000
(R) Monthly interest rate	.4%
(n) Total number of monthly payments remaining	360
(M) Monthly payment	

After adjustment

Component	Cost
(P) Principal	$187,000
(R) Monthly interest rate	(4.8 → 6.0) .5%
(n) Total number of monthly payments remaining	336
(M) Monthly payment	

Adjustable-Rate Mortgages: Pros and Cons

Pros

- Lenders often give borrowers lower ______ interest rates.
- A drop in interest rates could mean lower monthly payments.

Cons

- A rise in interest rates would mean ______ monthly payments.
- Higher monthly payments could mean a larger overall payment.

Adjustable-rate mortgages carry more of a ______ for borrowers.

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Balloon Payment Mortgages

In a balloon payment mortgage, the majority of the principal is due in [ ] payment.

- The borrower agrees to make regular payments for a [ ] term (often between five and ten years).
- The borrower pays interest and repays some of the principal.
- At the end of the term, the remaining principal is due [ ].

Sample Balloon Payment

Component	Cost
Principal	$200,000
Monthly interest rate	.333%
Monthly payment	$954
Total interest paid	$52,286
Total principal paid	$26,296
Remaining payment	**$** [ ]

Sample Terms

Loan amount: $200,000

Regular payment term: 7 years

Fixed rate interest: 4.0%

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Balloon Payment Mortgages: Pros and Cons

Pros

- It can allow the borrower to ________ some of the expense of buying a house.
- It can be a good choice for a borrower who plans to sell the home ________ the term is over.

Cons

- A borrower may ________ the home and equity if unable to afford the final balloon payment.

Balloon payment mortgages are useful for certain borrowers.

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Lesson Question

What factors do home buyers need to consider when taking on a mortgage?

Answer

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Review: Key Concepts

There are many factors that need to be taken into consideration when buying a home.

Components of a mortgage

- Principal
-
- Fees
-
- Points

Types of mortgages

- rate
- Adjustable rate
- payment

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Use this space to write any questions or thoughts about this lesson.