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# Should you Trade your Adjustable Rate for a Fixed Rate Mortgage?

Many, many Americans rushed to become part of the recent housing boom, taking advantage of initial low rate loans called Adjustable Rate Mortgages (ARMs.) Now that the housing boom has ended and home equity is not building up so quickly, some homeowners are wondering if it is time to switch out of their ARMs and into a fixed rate loan. If you fit into this category, there are several important factors you should consider in deciding what choice is best for you.

First of all, it is important to understand how an ARM loan works. Borrowers start out with a low interest rate on their loan, an interest rate that will remain constant for a period of 1, 3, 5, or 7 years. After the initial term is over, the interest rate on the loan (as well as the payment) will reset, usually at a higher rate. This is when the loan becomes “adjustable.” The rate can vary every so often based on the fluctuation of certain market indicators. If the economy keeps interest rate low, the adjustable rate may never cause you problems, but because you cannot predict the future of rates, payments may rise higher than you are comfortable. If you are rapidly approaching the resetting of your loan, you need to decide if you would be better off refinancing into a fixed rate loan.

One of the most important things to consider is how long you plan to stay in your current house. If you foresee a move in the near future, say five or so years, it may be more cost effective to simply stay with your present ARM loan until you sell your home. Even if you would be getting a better rate or payment schedule for that time with a fixed rate, you will have to pay new closing costs with the new refinance loan which may cost you more than the savings from the fixed rate. Talk with your mortgage professional to determine exactly how long you would have to stay in your home to make the switch profitable.

Of course if you are going to stay in your home long enough to make the refinance worthwhile, one of the greatest benefits to refinancing into a fixed rate loan is that you can avoid that steep payment jump. If you refinance in time you can take full advantage of the low interest rate with your ARM, and then switch before you experience the potentially unaffordable payment hikes.

Another great reason to refinance into a fixed rate loan is that your monthly mortgage payments will be completely predictable for the rest of your loan term. You get a fixed interest rate forever, a real perk if you enjoy stability. While the fixed rate may be higher than your initial ARM rate, it will never leave you wondering how much you will have to pay next month.

You should be careful though when refinancing because as mentioned before, it is an expensive process. In addition to new closing costs, the refinanced fixed rate loan totally resets your interest payments, increasing the amount of interest you’ll pay over the long run. Make sure the costs and benefits weigh in on your side before you jump into the new loan. In any case you should consult with your financial or mortgage advisor to talk out all the details of switching out of your adjustable rate mortgage.