10/28/2006

Mortgage Financing With Fixed Rate Loan Variations

If you are in the market for a mortgage, you have no doubt learned about the pros and cons of fixed rate loans. These are mortgages that allow you to lock in a rate for the entire course of your loan. You are probably familiar with the standard 30-year and 15-year fixed loans, but you may not have yet heard of the several fixed rate variations. These include the biweekly plan, balloon payment loans, and convertible fixed rate loans.

Biweekly Fixed Rate Loans

If you like the idea of shortening your loan, but do not have the cash to make the steep payments on a 15-year loan, you should look at a program that is a compromise between the 30-year and 15-year fixed loans. This is called the biweekly loan. This program includes a fixed rate, but instead of paying every month, you make payments every two weeks. Each payment is half of what you would have paid monthly, but since you pay biweekly, you end up making the equivalent of 13 months of mortgage payments in one year. It might not seem like one extra payment a year would make a big difference, but in reality the biweekly schedule will cut the length of your loan down to 18-22 years instead of 30.

The benefits are obviously that you pay off your mortgage sooner and own your home outright earlier. The disadvantages are that you will pay more money each year and that you will have fewer years of mortgage interest tax deductions. You might consider getting a traditional 30-year mortgage and simply putting that extra month’s payment into a high-yield savings account each year. Or get a 30-year fixed without a pre-payment penalty and simply make an extra payment every year or as often as you can afford. This way you are not locked into the larger payment schedule if it ever becomes too much for your budget.

Balloon Payment Fixed Rate Loans

Another form of fixed rate loans is the balloon payment. This type of mortgage financing provides for a loan term of 3, 5, or 7 years with payments similar to those of 30-year mortgages. The catch is that you are left with a very large chunk of the mortgage balance that will come due at the end of the term. You will have to either cough up the funds from your savings, or if that is not an option, you will have to refinance into a new loan. The benefit of a balloon payment loan is that you get low initial payments, and truly they are really designed to be refinanced at the end of the term. Fortunately, refinancing is a very popular program these days and you’ll probably be able to find a good deal on the new loan.

Convertible Fixed Rate Loans

Finally, you can explore the convertible fixed rate loan option, often known as a reduction option loan. This financing program allows for you to be able to drop the interest rate on your loan within a specified period of time, usually between the 13th and 59th month of your loan. So you may start out with a certain interest rate, but if the market rates drop down as much as 2% during the convertible stage of your loan, you can lock in that rate for the rest your mortgage term. At the time of converting you will have to pay some extra fees, possible even a half percent of your loan total. Still, this program can be great if you think the market rates will drop in the next year or two. If they don’t though, you will be stuck with a higher rate than you probably could have gotten with a normal 30-year fixed loan.

When it comes time to find mortgage financing, there are plenty of options out there. Once you have figured out the limitations of your financial situation, you may find that some variation of the fixed rate loan best fits your needs.

