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Learning to Adjust to Adjustable Rate Mortgages

If you have an adjustable rate mortgage (ARM) that is part of the $1 trillion worth of ARMs due to reset this year, you may be wondering how much your payments will change and if you will be able to afford them. “Payment shock” is a common complaint of many such borrowers. If it turns out the payments jump too high for you to afford, in a worst case scenario you might get behind on your payments, and ruin your credit by going into foreclosure. So to avoid all that mess and hassle, you can be deciding on your options before your interest rate resets. Consider either saving up now for the higher payments, refinancing your current loan or selling your house.

Start Saving Now

The first thing to do is to try to gauge how high your payments are likely to be after the reset. You can get a rough estimate by searching your loan contract for the published index that your rate is tied to. It may be an MTA, COFI, or CODI, or one of several other indices. You can look up the current value of your index online. Once you know the value, find the margin listed in your loan paperwork and add that amount to the current value. This will give an approximation of what your payments will be like. You should never be ‘shocked’ by your next payment jump because you have the power to monitor and track the index trends.

If you think you can probably manage the rate increase with a little belt-tightening, you should probably start now to set aside a little each month in anticipation of that payment hike. That way you will not be so hard-pressed to come up with extra funds later.

If you do not believe you will be able to afford the new payments, you may need to consider either selling your home or refinancing.

Refinance

If you are going to refinance or sell, realize that you need to make the decision and get started on the process before your payments increase and you start to get behind.

Refinancing may be the best option for you if you are planning to stay in your home long enough to make the upfront costs worth it. You will have to pay closing costs all over again with any new loan and they could total anywhere from 3% to 7% of the loan total.

Refinancing is also a good idea if you can actually find a better deal on a new loan. If you can find a fixed rate mortgage with a nice low rate or even a hybrid ARM that has long fixed periods, a refinance will be a wise choice. Refinancing your current mortgage will not be helpful if you do not get better terms and rates or if you truly cannot afford the home you are in. you do not want to have to refinance every couple years just to avoid payment increases; that will negate any equity you are building. If you cannot find a refinance loan that makes sense for you, your last option may be to sell and try to buy something that is really within your budget.

Sell

This is probably the least appealing option to you because you probably bought your house to be able to live in it, at least for several years. Yet if selling will help you avoid ruining your credit and losing your home to foreclosure it may be the best choice. It may be relatively easy to do you your home price has appreciated significantly since you bought it. If it has not, you may have to sell at a loss and pay off the rest of the mortgage with another loan. Remember though that this is still a better choice than having a foreclosure on your record.

Already Behind?

If you are reading this after your payments have skyrocketed and you are currently behind on your mortgage, you should immediately talk with your lender. You may still be able to work out a solution to avoid foreclosure. It is definitely in your mortgage lender's best interest to keep somehow save the loan, so most will be willing to create some sort of altered payment schedule to help you get back on track. Just do not delay any longer!

Adjustable rate mortgages can be a great help for getting you into a home. Unfortunately, sometimes they help some people get into homes they really cannot afford. If you fall in to this category, start planning now for how you can manage or avoid the pending rate and payment resets.