Regions Next Step Podcast

Home Ownership 101: Understanding an Adjustable Rate Mortgage

In this podcast, **Kreg Newman, a Mortgage Loan Officer for Regions Bank in Birmingham, Ala.**, discusses everything you need to know about adjustable rate mortgages.

Want to learn more about the following topics? Check out the link to hear from Kreg:

- Differences between a fixed-rate mortgage and an adjustable-rate mortgage (ARM)
- How to determine which type of mortgage is right for you

Episode Transcript

Narrator:
You're listening to the Next Step Podcast, "Understanding an Adjustable Rate Mortgage" – part of our Home Ownership 101 series presented by Regions Next Step – advice, tools and resources to help you get closer to reaching your unique financial goals.

When you're preparing to buy a home, you have two primary mortgage options: a fixed rate and adjustable rate mortgage. In this episode, we'll be discussing adjustable rate mortgages. Here to tell us what we need to know is Kreg Newman, Mortgage Loan Officer, with Regions Bank.

Kreg, to start, can you tell us what an adjustable rate mortgage is?

Kreg Newman:
Certainly, and thank you for having me. Now, just like it sounds, an adjustable-rate mortgage, otherwise known as an ARM, is a mortgage with rates that can change from time-to-time.

Usually, your interest rate, and therefore your monthly payment amount, will be locked in for a specific period like 5, 7 or 10 years. After that, the rate can fluctuate. This is because it will be tied to a standard index – like the SOFR rate – plus a margin, which is a fixed percentage rate you add to the standard index to obtain the new interest rate.

In contrast, the other primary mortgage option is a fixed-rate mortgage, which will have the same interest rate over the entire life of the loan.

Narrator:
It sounds like ARMs could be a good product for some people, so why do ARMs have such a negative connotation?

Kreg:
Previously, ARMs may have been fixed for a time period as little as 1, 6 or 12 months. Customers were taking a short-term approach by selecting these ARMs which had low teaser rates, then adjusted quickly. This caused financial hardship for some customers.

Today's ARMs have fixed rates for longer periods of time like 5, 7 or 10 years. After the fixed rate period, the rates begin to adjust periodically, such as every 6 months or annually, for the remainder of the loan.

Narrator:
So how can our listeners determine if an ARM is the right choice for them?

Kreg:
There are definitely a few things to consider. Which type is right for you will depend on factors like how comfortable you are with risk, and how long you plan to stay in the home. The key is to pick a product that matches the duration of the time you expect to own the property. For example, if you plan to own your home for 5 years based on your future needs, then a 7-year ARM is a great product and gives you a cushion.

Narrator:
After the fixed rate period is over, how is the rate determined and how high can it go?

Kreg:
First, the rate can decrease or increase. The amount of the change is determined by the standard index at the time of the adjustment plus the margin. The good news is ARMs have caps or limits on the amount the rate can change both annually and over the life of the loan. For example, most ARMs have a lifetime cap or limit of 5 percentage points over the initial fixed rate.

Narrator:
At the end of the day, we still need to make sure we can afford the payments should the rate increase if we end up staying longer than we thought we would.

Kreg:
Yes. A fixed rate mortgage is always the most conservative choice. It really pays to be completely aware of how ARMs work and determine if that is a suitable product choice for you.

Narrator:
Well thank you, Kreg, for taking us through the ins-and-outs of adjustable rate mortgages.

You can also find additional resources including articles, checklists, calculators and more online at www.regions.com/nextstep. No matter your goals, Regions will help you with each step you want to take. Thank you for listening.