# Selling in a Rising Rate Market

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# What is an adjustable-rate mortgage (ARM)?

An adjustable-rate mortgage, or **ARM**, is a home loan with an interest rate that can change periodically. This means that the monthly payments can go up or down.

After introductory rate, the rate adjusts based on the combination of the **margin** on the loan plus current **index** and not to exceed the **cap** or max adjustment allowed.



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# Margin

- **Fixed percentage rate** that is added to an index value to determine the **fully indexed interest rate** of an ARM
- **Constant** throughout the life of the mortgage

# Index

- Reflects the **cost of money** and is based on published independent interest rates (CMT; COFI, SOFR, etc.)
- The Index is based on **current market conditions**



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# Cap

- **Safeguards** established at the inception of the loan and **never change**
- **Initial cap** is the **maximum amount** an interest rate can adjust immediately after the fixed-rate period
- **Periodic cap** is the **maximum** a **rate** can **increase or decrease** at any given rate change
- **Life cap** sets the **limit** of the **maximum interest** rate that can be charged on the loan

# Types of ARMs

## 1 yr.

Rate adjusts annually

## 3/1

Rate is fixed for 3 years, then adjusts each year for the remaining 27-year term

## 3/3

Rate is fixed for 3 years, then adjusts every 3 years for the remaining 27-year term

## 5/1

Rate is fixed for 5 years, then adjusts each year for the remaining 25-year term

## 7/1

Rate is fixed for 7 years, then adjusts each year for the remaining 23-year term

## 10/1

Rate is fixed for 10 years, then adjusts each year for the remaining 20-year term

# How do ARMs work?

| Fannie Mae Qualifying Interest Rate Requirements | |
|---|---|
| Transaction Type | DU and Manual Underwriting |
| ARMs with an initial fixed-rate period of 3 years or less | The maximum interest rate that could apply during the first 5 years after the first payment is due |
| ARMs with an initial fixed-rate period of 5 years | Greater of the note rate plus 2% or the fully indexed rate |
| ARMs with an initial fixed-rate period of greater than 5 years | Greater of the note rate or the fully indexed rate |

| Radian ARM Payment Qualification | | |
|---|---|---|
| Transaction Type | DU and Manual Underwriting | |
| ARMs with an initial fixed period less than 5 years | Qualify using the higher of the Note Rate plus 2% or the Fully Indexed | Temporary Buy Down Not Included in Qualifying Payment Calculation |
| ARMs with an initial fixed period of 5 years or greater | Starting Note Rate | |

# 5/6m ARM Example

## Formula: Index + Margin = New Rate

Initial Rate: 4.125%

Margin: 2%

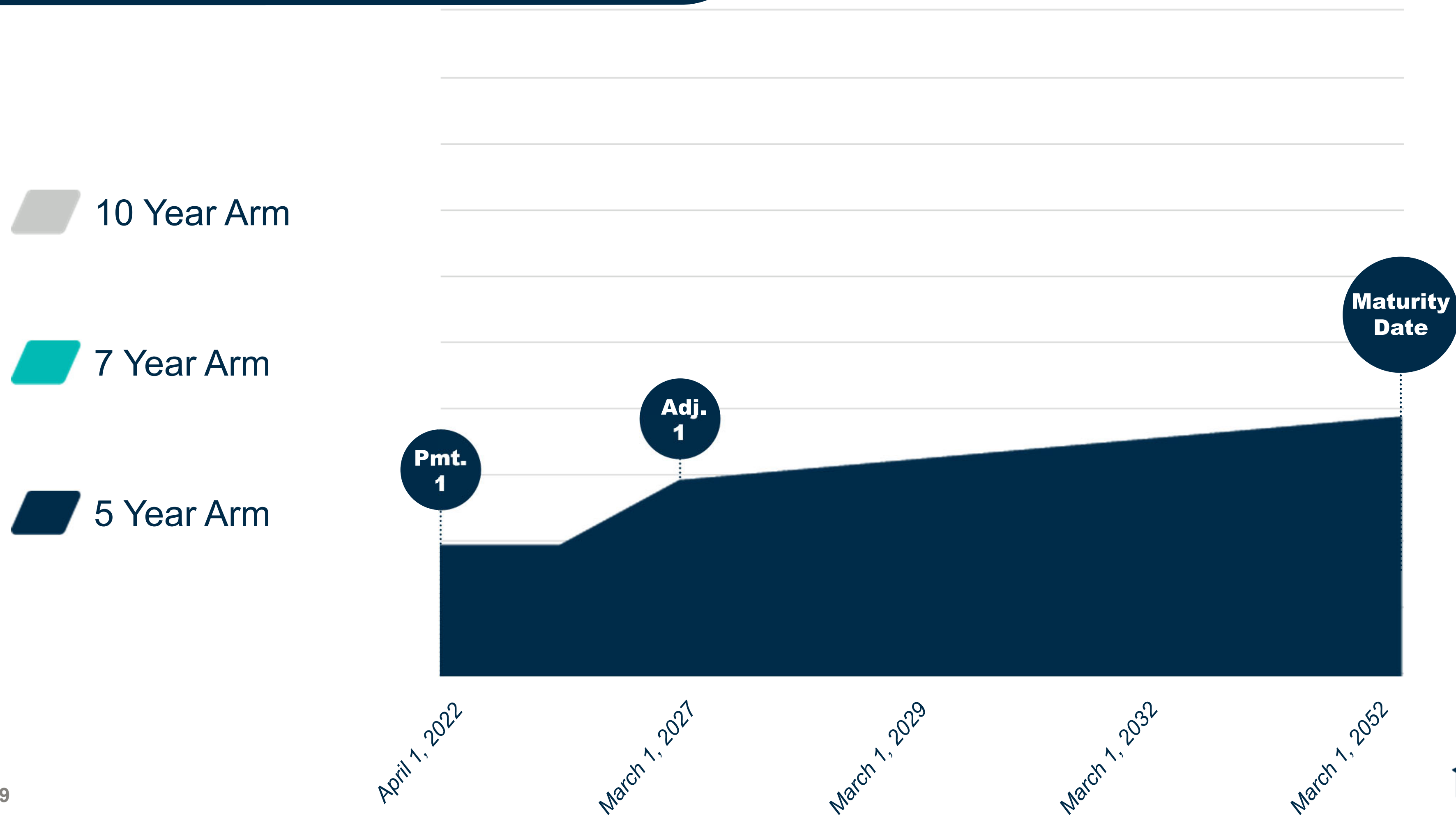
Periodic Cap: 2%

Life Cap: 6%

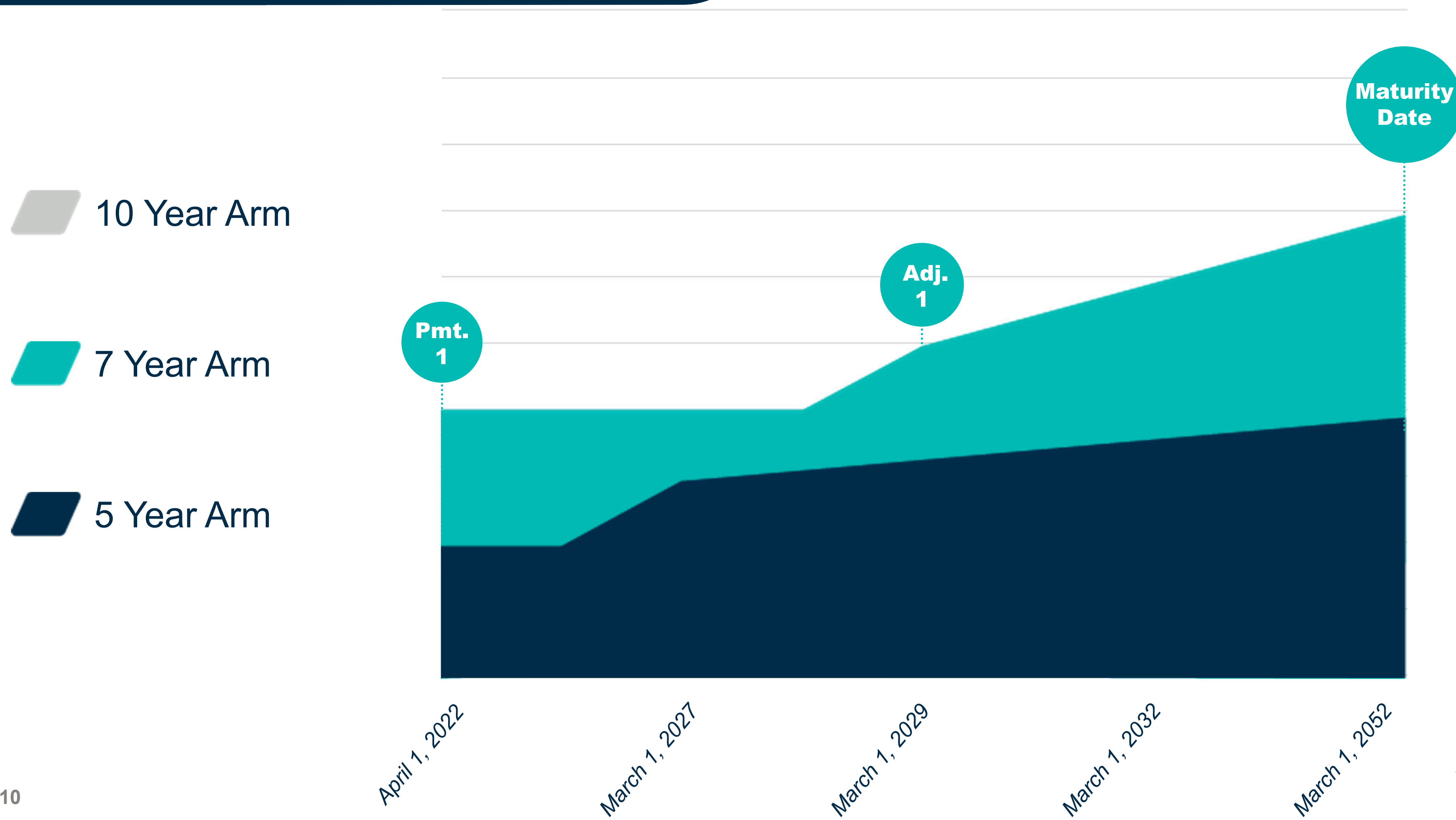
*(or 10.125% for this loan)*

| Period | Index Value | Margin | Index + Margin | New Rate |
|---|---|---|---|---|
| **Start** | 3% | 2.0% | 5.0% | 4.125% |
| 1st Adjustment | 4% | 2.0% | 6.0% | 6.0% |
| 2nd Adjustment | 7% | 2.0% | 9.0% | 8.0% |
| 3rd Adjustment | 10% | 2.0% | 12.0% | 10.0% |
| 4th Adjustment | 10% | 2.0% | 12.0% | 10.125% |

# 5, 7, & 10 Year ARM Examples



# 5, 7, & 10 Year ARM Examples



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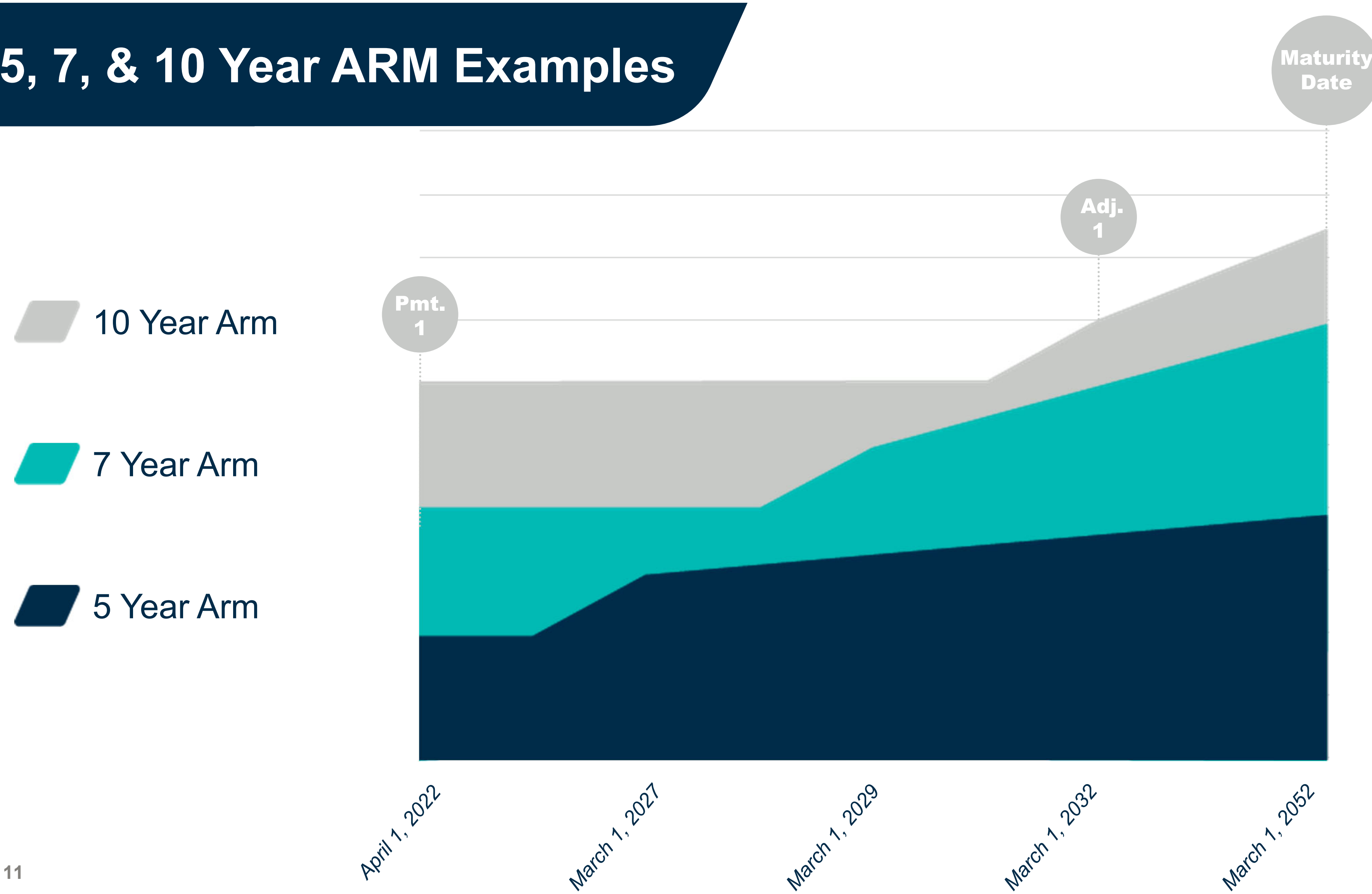
# 5, 7, & 10 Year ARM Examples



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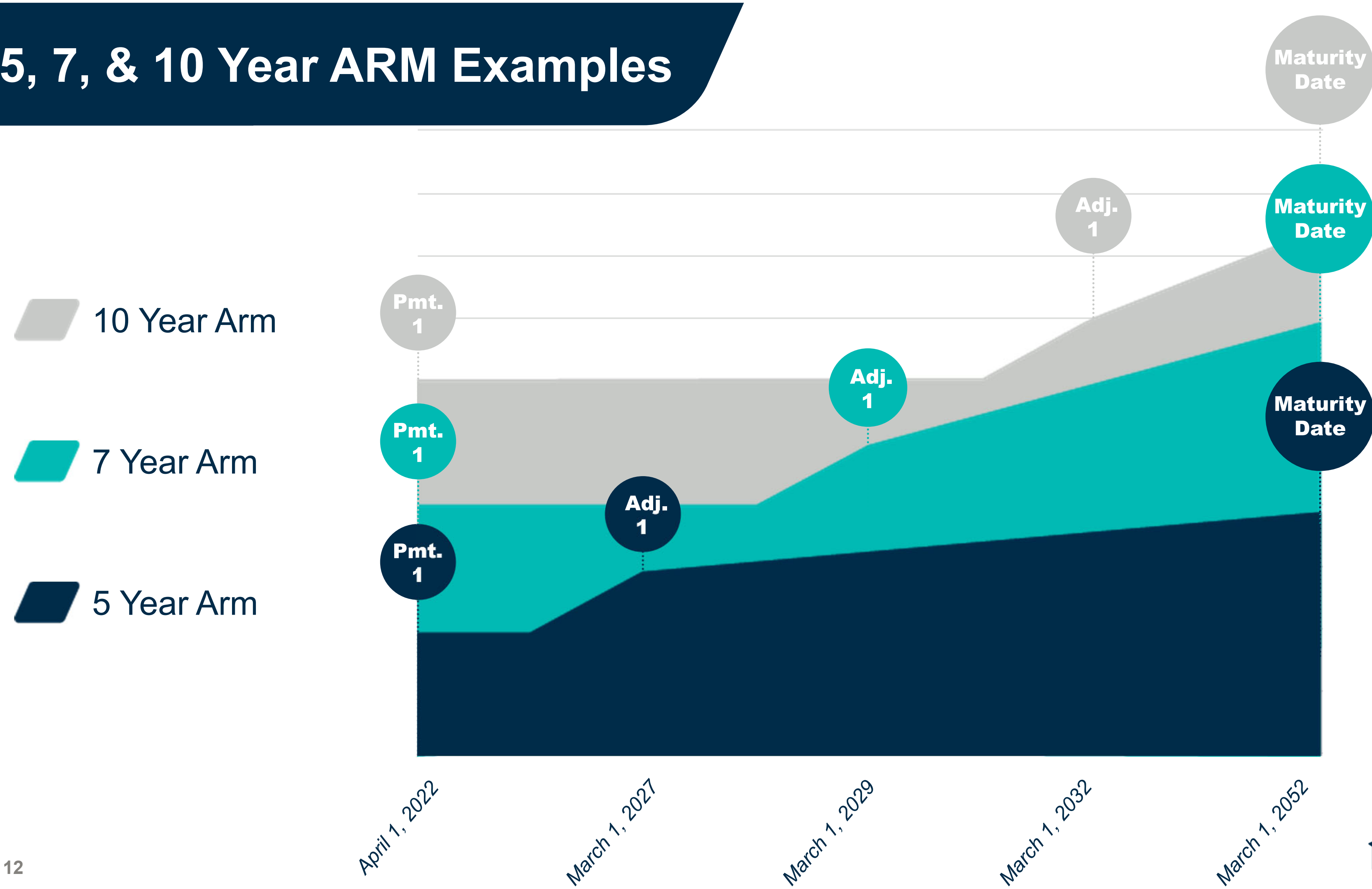
# 5, 7, & 10 Year ARM Examples



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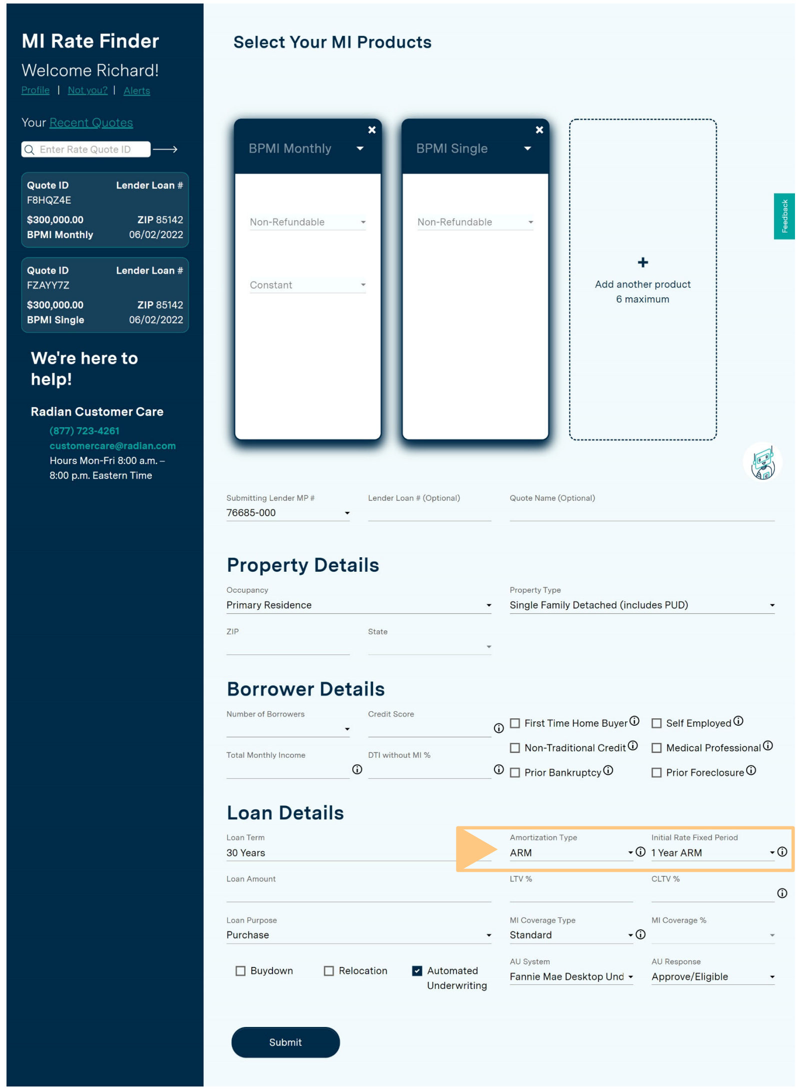
# Mortgage Insurance



# Important Items on Adjustable-Rate Note

**ADJUSTABLE RATE NOTE**
(1 Year Treasury Index    Rate Caps)

**THIS NOTE CONTAINS PROVISIONS ALLOWING FOR CHANGES IN MY INTEREST RATE AND MY MONTHLY PAYMENT. THIS NOTE LIMITS THE AMOUNT MY INTEREST RATE CAN CHANGE AT ANY ONE TIME AND THE MINIMUM AND MAXIMUM RATES I MUST PAY.**

____________, ______    ____________, ______
[Date]    [City]    [State]

______________________________
[Property Address]

**1. BORROWER'S PROMISE TO PAY**

In return for a loan that I have received, I promise to pay U.S. $__________ (this amount is called "Principal"), plus interest, to the order of the Lender. The Lender is ______________________. I will make all payments under this Note in the form of cash, check or money order.

I understand that the Lender may transfer this Note. The Lender or anyone who takes this Note by transfer and who is entitled to receive payments under this Note is called the "Note Holder."

**2. INTEREST**

Interest will be charged on unpaid principal until the full amount of Principal has been paid. I will pay interest at a yearly rate of ______%. The interest rate I will pay will change in accordance with Section 4 of this Note.

The interest rate required by this Section 2 and Section 4 of this Note is the rate I will pay both before and after any Survival Event as defined in this Note.

**3. PAYMENTS**

**(A) Time and Place of Payments**

I will pay principal and interest by making a payment every month.

I will make my monthly payment on the first day of each month beginning on __________, ______. I will make these payments every month until I have paid all of the principal and interest and any other charges described below that I may owe under this Note. Each monthly payment will be applied as of its scheduled due date and will be applied to interest before Principal. If, on __________, ______, I still owe amounts under this Note, I will pay those amounts in full on that date, which is called the "Maturity Date." I will continue to pay those amounts both before and after any Survival Event as defined in this Note, until I have paid all of the principal and interest and any other charges described below that I may owe under this Note.

I will make my monthly payments at ______________________ or at a different place if required by the Note Holder.

**(B) Amount of My Initial Monthly Payments**

Each of my initial monthly payments will be in the amount of U.S. $__________. This amount may change.

**(C) Monthly Payment Changes**

Changes in my monthly payment will reflect changes in the unpaid principal of my loan and in the interest rate that I must pay. The Note Holder will determine my new interest rate and the changed amount of my monthly payment in accordance with Section 4 of this Note.

**4. INTEREST RATE AND MONTHLY PAYMENT CHANGES**

**(A) Change Dates**

The interest rate I will pay may change on the first day of __________, ______, and on that day every 12th month thereafter. Each date on which my interest rate could change is called a "Change Date."

**(B) The Index**

Beginning with the first Change Date, my interest rate will be based on an Index. The "Index" is the weekly average yield on United States Treasury securities adjusted to a constant maturity of one year, as made available by the Federal Reserve Board. The most recent Index value available as of the date 45 days before each Change Date is called the "Current Index," provided that if the Current Index is less than zero, then the Current Index will be deemed

## Change Date

**The interest rate I will pay may change on the first day of**

**______________, ________,**

**and on that day every 12th month thereafter. Each date on which my interest rate could change is called a "Change Date."**





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# Important Items on Adjustable-Rate Note

to be zero for purposes of calculating my interest rate.

If the Index is no longer available, the Note Holder will choose a new index which is based upon comparable information. The Note Holder will give me notice of this choice.

**(C) Calculation of Changes**

Before each Change Date, the Note Holder will calculate my new interest rate by adding percentage points ( %) (the "Margin") to the Current Index. The Note Holder will then round the result of this addition to the nearest one-eighth of one percentage point (0.125%). Subject to the limits stated in Section 4(D) below, this rounded amount will be my new interest rate until the next Change Date.

The Note Holder will then determine the amount of the monthly payment that would be sufficient to repay the unpaid principal that I am expected to owe at the Change Date in full on the Maturity Date at my new interest rate in substantially equal payments. The result of this calculation will be the new amount of my monthly payment.

**(D) Limits on Interest Rate Changes**

The interest rate I am required to pay at the first Change Date will not be greater than ______ % or less than ______ %. Thereafter, my interest rate will never be increased or decreased on any single Change Date by more than one percentage point (1.0%) from the rate of interest I have been paying for the preceding 12 months. My interest rate will never be greater than ______ % or less than the Margin.

**(E) Effective Date of Changes**

My new interest rate will become effective on each Change Date. I will pay the amount of my new monthly payment beginning on the first monthly payment date after the Change Date until the amount of my monthly payment changes again.

**(F) Notice of Changes**

The Note Holder will deliver or mail to me a notice of any changes in my interest rate and the amount of my monthly payment before the effective date of any change. The notice will include information required by law to be given to me and also the title and telephone number of a person who will answer any question I may have regarding the notice.

**5. BORROWER'S RIGHT TO PREPAY**

I have the right to make payments of Principal at any time before they are due. A payment of Principal only is known as a "Prepayment." When I make a Prepayment, I will tell the Note Holder in writing that I am doing so. I may not designate a payment as a Prepayment if I have not made all the monthly payments due under the Note.

I may make a full Prepayment or partial Prepayments without paying a Prepayment charge. The Note Holder will use my Prepayments to reduce the amount of Principal that I owe under this Note. However, the Note Holder may apply my Prepayment to the accrued and unpaid interest on the Prepayment amount, before applying my Prepayment to reduce the Principal amount of the Note. If I make a partial Prepayment, there will be no changes in the due dates of my monthly payment unless the Note Holder agrees in writing to those changes. My partial Prepayment may reduce the amount of my monthly payments after the first Change Date following my partial Prepayment. However, any reduction due to my partial Prepayment may be offset by an interest rate increase.

**6. LOAN CHARGES**

If a law, which applies to this loan and which sets maximum loan charges, is finally interpreted so that the interest or other loan charges collected or to be collected in connection with this loan exceed the permitted limits, then: (a) any such loan charge shall be reduced by the amount necessary to reduce the charge to the permitted limit; and (b) any sums already collected from me which exceeded permitted limits will be refunded to me. The Note Holder may choose to make this refund by reducing the Principal I owe under this Note or by making a direct payment to me. If a refund reduces Principal, the reduction will be treated as a partial Prepayment.

**7. BORROWER'S FAILURE TO PAY AS REQUIRED**

**(A) Late Charges for Overdue Payments**

If the Note Holder has not received the full amount of any monthly payment by the end of calendar days after the date it is due, I will pay a late charge to the Note Holder. The amount of the charge will be ______ % of my overdue payment of principal and interest. I will pay this late charge promptly but only once on each late payment.

**(B) Default**

If I do not pay the full amount of each monthly payment on the date it is due, I will be in default.

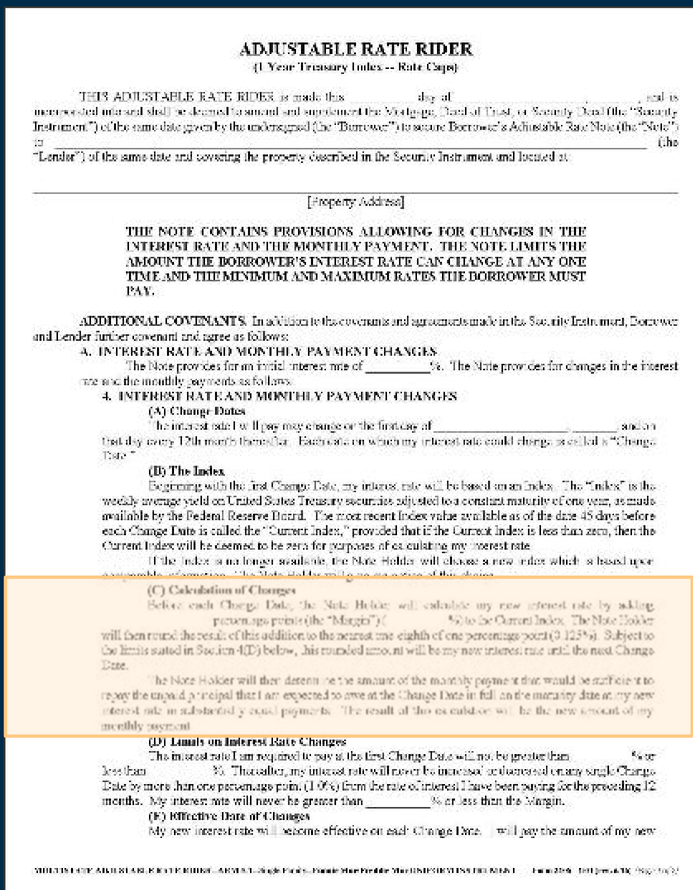
**(C) Notice of Default**

If I am in default, the Note Holder may send me a written notice telling me that if I do not pay the overdue

## Effective Date of Changes

**My new interest rate will become effective on each Change Date. I will pay the amount of my new monthly payment beginning on the first monthly payment date after the Change Date until the amount of my monthly payment changes again.**

# Important Items on Rider



**ADJUSTABLE RATE RIDER**
(1 Year Treasury Index -- Rate Caps)

THIS ADJUSTABLE RATE RIDER is made this ______ day of ______, ______, and is incorporated into and shall be deemed to amend and supplement the Mortgage, Deed of Trust, or Security Deed (the "Security Instrument") of the same date given by the undersigned (the "Borrower") to secure Borrower's Adjustable Rate Note (the "Note") to ______________________ (the "Lender") of the same date and covering the property described in the Security Instrument and located at:

______________________
[Property Address]

**THE NOTE CONTAINS PROVISIONS ALLOWING FOR CHANGES IN THE INTEREST RATE AND THE MONTHLY PAYMENT. THE NOTE LIMITS THE AMOUNT THE BORROWER'S INTEREST RATE CAN CHANGE AT ANY ONE TIME AND THE MINIMUM AND MAXIMUM RATES THE BORROWER MUST PAY.**

**ADDITIONAL COVENANTS.** In addition to the covenants and agreements made in the Security Instrument, Borrower and Lender further covenant and agree as follows:

**A. INTEREST RATE AND MONTHLY PAYMENT CHANGES**

The Note provides for an initial interest rate of ________%. The Note provides for changes in the interest rate and the monthly payments as follows:

**4. INTEREST RATE AND MONTHLY PAYMENT CHANGES**

**(A) Change Dates**

The interest rate I will pay may change on the first day of ______________, ______, and on that day every 12th month thereafter. Each date on which my interest rate could change is called a "Change Date."

**(B) The Index**

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If the Index is no longer available, the Note Holder will choose a new index which is based upon comparable information. The Note Holder will give me notice of this choice.

**(C) Calculation of Changes**

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The Note Holder will then determine the amount of the monthly payment that would be sufficient to repay the unpaid principal that I am expected to owe at the Change Date in full on the maturity date at my new interest rate in substantially equal payments. The result of this calculation will be the new amount of my monthly payment.

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**(E) Effective Date of Changes**

My new interest rate will become effective on each Change Date. I will pay the amount of my new

## Calculation of Changes

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**The Note Holder will then determine the amount of the monthly payment that would be sufficient to repay the unpaid principal that I am expected to owe at the Change Date in full on the maturity date at my new interest rate in substantially equal payments. The result of this calculation will be the new amount of my monthly payment.**



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# ARM vs. Fixed-Rate Loan

## When does it make sense for your borrower?

# ARM vs. Fixed-Rate Loan

| ARM | Fixed Rate |
|---|---|
| Lower rates/payments early in the term, possibly allowing customer to purchase larger home | Rates and payment stay consistent – no surprises or inflation |
| May benefit short-term homeowner (# of years) | Good for borrower planning to purchase "forever home" |
| Helps customer save and invest more money up front | Simple to understand |

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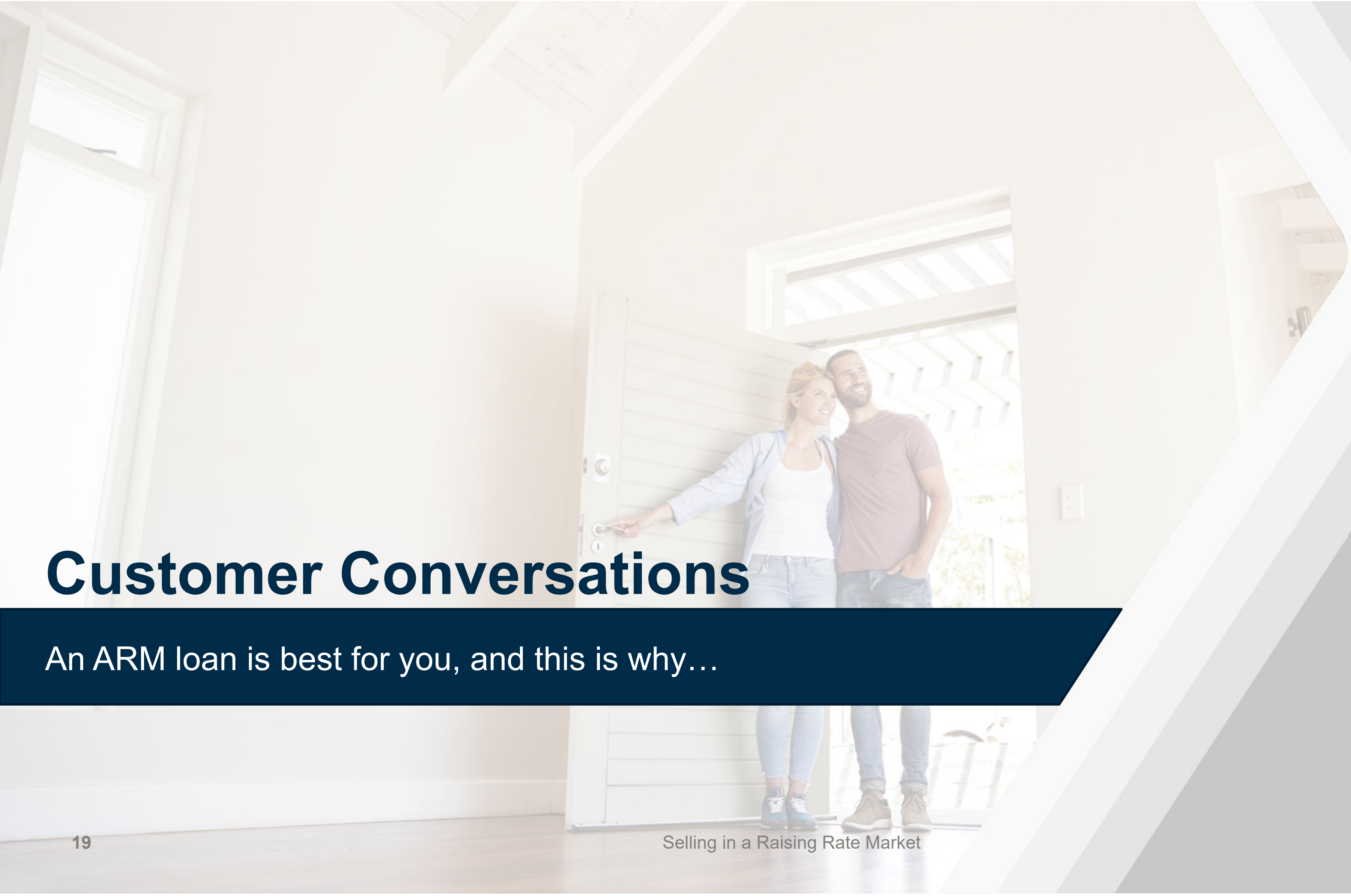
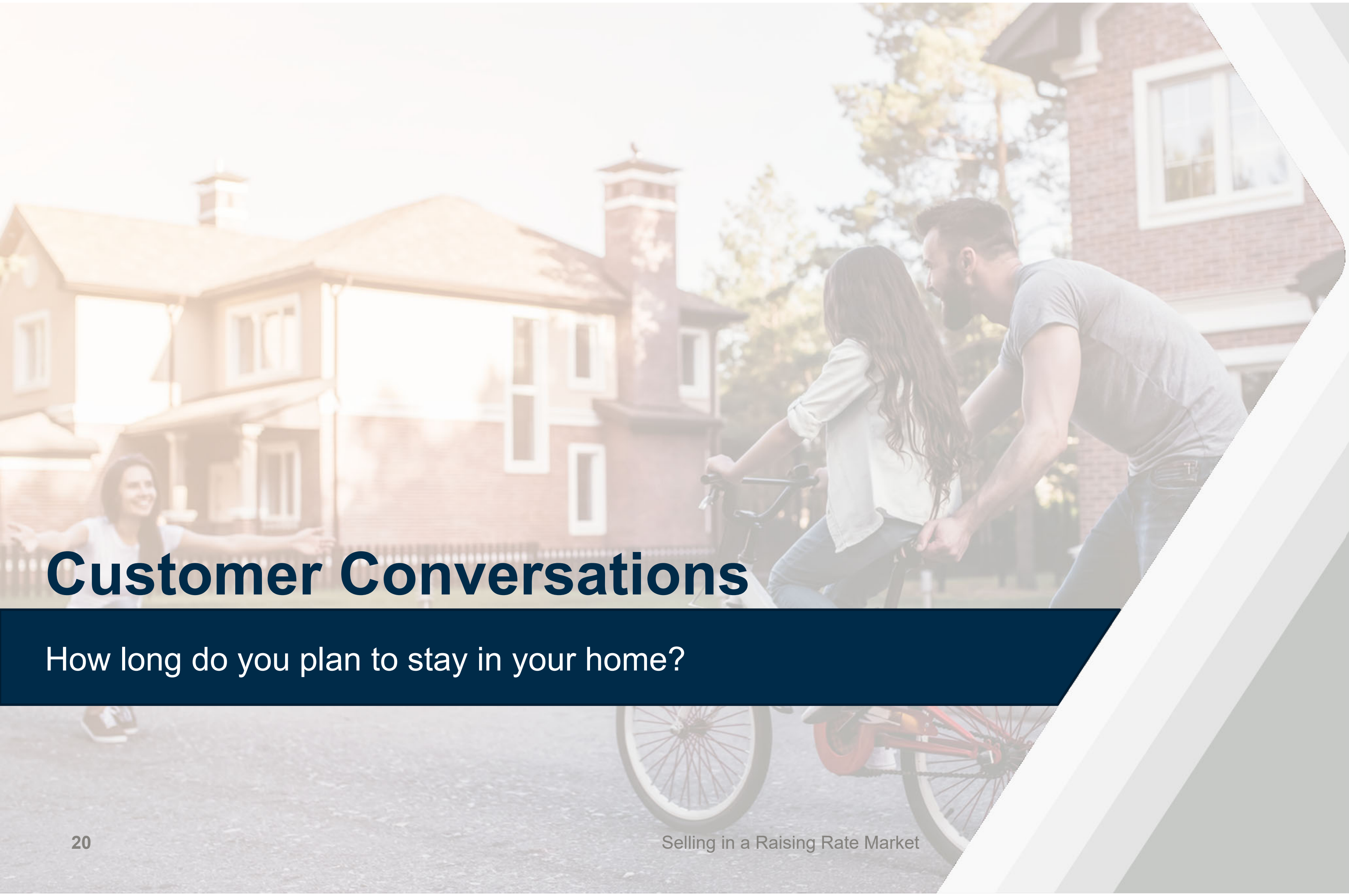


# Customer Conversations

An ARM loan is best for you, and this is why…



# Customer Conversations

How long do you plan to stay in your home?



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# Customer Conversations

Let's discuss how your rate will adjust over the term of the loan.

# Customer Conversations

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