



UNIT 7 – Overview

Securing a Home Mortgage

When most people purchase a home, they are buying the single biggest and most valuable asset they will ever own. So, don't jump right into it and expect that you will have all of the answers you need in a few hours. Instead, be prepared to do a lot of research, ask a lot of questions, and spend a lot of time. After all, if a home is the largest asset you will ever purchase, it is also the single most expensive thing you will ever buy, so take the time to look around, evaluate your options, and make the best choice you possibly can. In the end, the time you invest on the front end will be well worth the trouble.

There are a number of ways to secure a home mortgage. Some people work with their local bank, some work with mortgage brokers, and some look on the internet. All of these approaches are legitimate, but it's a good idea to pursue each so that you know the advantages and disadvantages of each.

First-time homeowners are often surprised to see how different one mortgage appears to be much from another – but there is a good reason for this, and the reason is price. For example, the bottom line is that the mortgage is really no more than a loan to the homeowner with the home being kept as collateral. If all mortgages were **homogeneous products**, or products that were exactly the same, however, then lenders would have to compete with one another on the basis of price, and the lender offering the lowest price would issue the most mortgages.

To avoid competing on price alone, lenders like to offer **differentiated products**, or products that have been amended in some minor or even major way to make it appear different from a competitor's mortgage. If a lender can successfully differentiate his mortgage from a competitor's, it is easier to charge a higher price. If all lenders are doing the same thing, it is even more difficult for a borrower to compare mortgages and to find the one with the best price, and so the borrower can easily end up with a higher-priced mortgage rather than a lower-priced one.



Unit Objectives:

- Explain how to secure a home mortgage.
- Understand the components of financing a home mortgage.
- Evaluating different types of mortgages.

Key Concepts:

- **Closing costs:** the sum of the individual fees charged by a lender
- **Differentiated products:** Products which have real or perceived differences so that the seller can charge a slightly higher price.
- **Down payment:** Initial payment made when securing a mortgage to reduce the lender's exposure to risk; computed as a percentage of the total loan value
- **Graduated payment mortgage (GPM):** mortgage that has a low initial payment during the early years of the mortgage. The payments rise gradually and then level off for the remainder of the loan.
- **Growing equity mortgage (GEMs):** mortgages designed for borrowers who want to pay the loan off early by having equity in the loan grow as fast as possible.
- **Homogeneous products:** Products which, for all practical purposes, are virtually identical
- **Interest only mortgages (I-O):** mortgages which have an initial period of about 5 years during which the monthly payment only covers the interest on the loan. When the initial period is over, the payment increases so that the principal can eventually be paid off.
- **Mortgage securitization:** Process of bundling mortgages for the purpose of creating an income-generating asset against which a bond can be issued.
- **Securitizing mortgages:** turning a bundle of mortgages into an income-earning asset
- **Teaser rate:** an unrealistically low introductory rate which like many introductory credit card offers
- **Points:** an amount charged by the lender. One point is one percent of the loan.

