





# 4 - Fixed Rate Mortgage - ch. 4

🔍 course	MGMT 170
📁 area	ucla
🕒 created	@April 10, 2023 10:55 AM
🕒 updated	@June 15, 2023 10:07 AM
➤ <input checked="" type="checkbox"/> tasks	
➤  courses	 <u>MGMT 170: Real Estate Finance</u>
🔗 URL	
📌 tags	

## Definitions

### ▼ point

- ▼ a 1% charge on a loan - usually used to collect payment up front

### ▼ monthly payments (PMT)

- ▼ usually pay monthly interest + some principal (amortization)

### ▼ arm

- ▼ adjustable rate mortgage

### ▼ debt service constant

- ▼ rate of payment - interest + amortization rates

## Resources

[https://s3-us-west-2.amazonaws.com/secure.notion-static.com/df90a7f7-def1-4b18-b0de-46e66fec9464/FIXED\\_RATE\\_MORTGAGES\\_-\\_Chapter\\_4.pdf](https://s3-us-west-2.amazonaws.com/secure.notion-static.com/df90a7f7-def1-4b18-b0de-46e66fec9464/FIXED_RATE_MORTGAGES_-_Chapter_4.pdf)

- ▼ when debt service constant =  
interest → interest only loan → PV  
= FV = loan amount
- ▼ CPM
  - ▼ constant payment loan - pay
- ▼ annuity
  - ▼ a guaranteed payment to you -  
accumulates over time
- ▼ free and clear
  - ▼ free and clear of debt
  - ▼ promissory note fulfilled
  - ▼ security instrument (deed of  
trust/mortgage) extinguished

## Big Ideas

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### ▼ Lecture

- ▼ Capital Markets
  - ▼ financial and securities  
markets - includes mortgage  
market
- ▼ loan availability
  - ▼ supply/cost of mortgage funds  
- affected by economic growth  
(global, national, local),  
expected Inflation, and other  
Risks
- ▼ lenders as intermediaries

- ▼ most real estate lenders (mortgage providers, banks) sell their loans into the secondary mortgage market instead of holding loans to maturity
- ▼ loan pricing
  - ▼ interest rate, fees, points and costs charged by lender, and loan terms (e.g. prepayment penalties)
- ▼ real interest rate
  - ▼ nominal/contract interest rate MINUS expected inflation
- ▼ risk adjusted return
  - ▼ expected return relative to expected risk
- ▼ amortization
  - ▼ process of repaying the loan (principal) balance over time
- ▼ balloon payment
  - ▼ principal balance due on the maturity date
- ▼ pay rate vs. accrual rate
  - ▼ pay rate is true monthly payment made by a Borrower against the loan  $\geq$  accrued interest due on the loan
- ▼ constant payment mortgage (CPM)

- ▼ when monthly payments are constant - loan is fully/partially/negative amortizing, or interest only
- ▼ constant amortizing mortgage (CAM)
  - ▼ when each monthly payment has constant amortization (principal payment) → monthly payment and interest accrued are decreasing → you pay less interest overall than CPM
- ▼ reverse annuity mortgage (RAM)
  - ▼ lender sends fixed monthly checks to borrower who pays back accumulated principal and accrued interest
  - ▼ targeted at seniors who have paid off their loans but cannot stay/afford to stay in the home → allows borrowers/owners to convert equity into periodic income/cash
  - ▼ the loan is to be repaid when the house is old, the borrower dies, or by heirs
- ▼ loan fees and costs
  - ▼ origination fees (for loan writing and processing), appraisal and credit report
  - ▼ loan fees and points increase the lender's yield (return)

- ▼ annual percentage rate (APR)
  - ▼ discloses effects of loan fee, points, and costs on residential loans (assuming held to maturity)
- ▼ truth-in-lending act
  - ▼ fred regulation Z requires lenders to include all fees, points, costs in APR (NOT prepayment penalties)
- ▼ prepayment penalties
  - ▼ increase the effective yield to lender - subject to negotiation, not reflected in APR
- ▼ effective annual interest rate
  - ▼ calculation that considers all loan fees, points, costs, and any prepayment penalties actually paid
  - ▼ → only affected by time the loan is held until (full) repayment



## SUMMARY