

# Lots of interest. Little Principal

Why do I pay so much interest in the early years of a mortgage loan?

The interest owed starts to accrue from the day the loan is made. When you deposit money at the bank, you naturally expect to start earning interest on the balance right away. It's exactly the same for lenders; they expect to earn interest on the balance as soon as they make a loan.

Interest diminishes along with the loan balance. On a typical loan, you pay principal each month, which reduces the loan balance and interest owed.

## Example:

Loan Amount	\$250,000
30-Year Fixed Rate	5.0%
Monthly Principal & Interest Payment	\$1,342
Interest Paid in First Year	\$12,416
Principal Paid in First Year	\$3,688

Note: This is just an example. It is not an offer to lend nor intended to represent a current interest rate.

You enjoy a fixed payment. For a fixed-rate loan, payments are calculated to remain the same throughout the loan term. As the amount you owe in interest each month declines, you are able to pay more toward principal with the same payment amount.

Mortgages remain affordable. Paying interest owed plus a small amount of principal each month in the early years of a loan contributes to affordability. If the amounts of principal and interest were equal from the beginning, the payment would be substantially higher, and fewer people would qualify.

## Can I tip the scales?

Almost every loan allows you to pay extra principal with your monthly payment. While paying extra will not reduce future months' fixed payments, it will reduce the term of your loan. If you sell or refinance before the full loan term—which most borrowers do—you will have more equity in your home than you would otherwise. You can also reduce interest payments by using a shorter term loan, such as a 20-year rather than a 30-year.

If you have any questions about whether your loan allows you to pay extra principal and how those payments will impact your loan, please ask me. I am happy to help.



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