

You are considering a 5/1 ARM and a 30 Year fixed rate mortgage to finance your property. The loan will be for \$400,000. The ARM has closing costs of \$5561 and an APR of 2.625%. It has an annual interest rate cap of 2% and a lifetime cap of 5%. The fixed rate has closing costs of \$4314 and an APR of 4%. You do not plan to make any early prepayments, unless you sell the house.

- a. Assuming a worst case scenario for interest rates, what is the effective cost for each loan and which loan is preferred if you anticipate selling the home in 5 years.
- b. Assuming a worst case scenario for interest rates, what is the effective cost for each loan and which loan is preferred if you anticipate selling the home in 10 years.
- c. Assuming a worst case scenario for interest rates, what is the effective cost for each loan and which loan is preferred if you anticipate keeping the home at least 30 years.