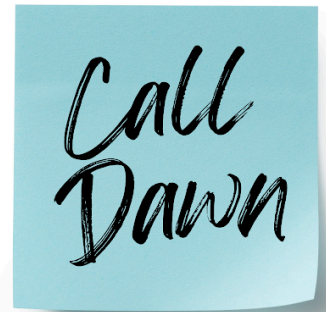




What is a Balloon Payment?

A **balloon payment** refers to a large lump-sum payment made at the end of a loan term, in addition to the regular minimum monthly installments. This type of payment is often associated with private mortgages, where a seller or family member acts as the lender, and may require periodic balloon payments. For instance, a loan might allow for interest-only monthly payments but necessitate a balloon payment of \$10,000 each January 1st. Private loans can have unique structures like this.



Even traditional bank mortgages can involve balloon payments. Most loans are fully amortized, meaning the minimum monthly payment is designed to pay off the loan by the end of its term. In contrast, loans with a balloon payment feature do not align monthly payments with the loan term. For example, a loan might have a monthly payment based on a 30-year term, but any remaining balance is due as a balloon payment after 7 years, a common time frame for such arrangements. If you haven't sold your home or paid off your mortgage by the time the balloon payment is due, you will need to refinance.

Another option is the "5/25" or "7/23" loan, where the minimum payment is based on a 30-year term, but the balloon payment allows for a built-in refinance. This refinance occurs at a market-based interest rate, similar to an adjustable-rate mortgage (ARM), but unlike an ARM, the rate adjusts only once and then remains fixed for the loan's duration. Although there are conditions for this built-in refinance—such as a good payment history and continued occupancy—this can be a more cost-effective and convenient alternative to standard refinancing.

However, balloon loans are becoming increasingly rare, as both consumers and the secondary mortgage market show diminishing interest in these products. Regulatory changes may lead to their decline, as loans with a balloon payment feature do not qualify as Qualified Mortgages (QM) under the Truth in Lending Act.

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