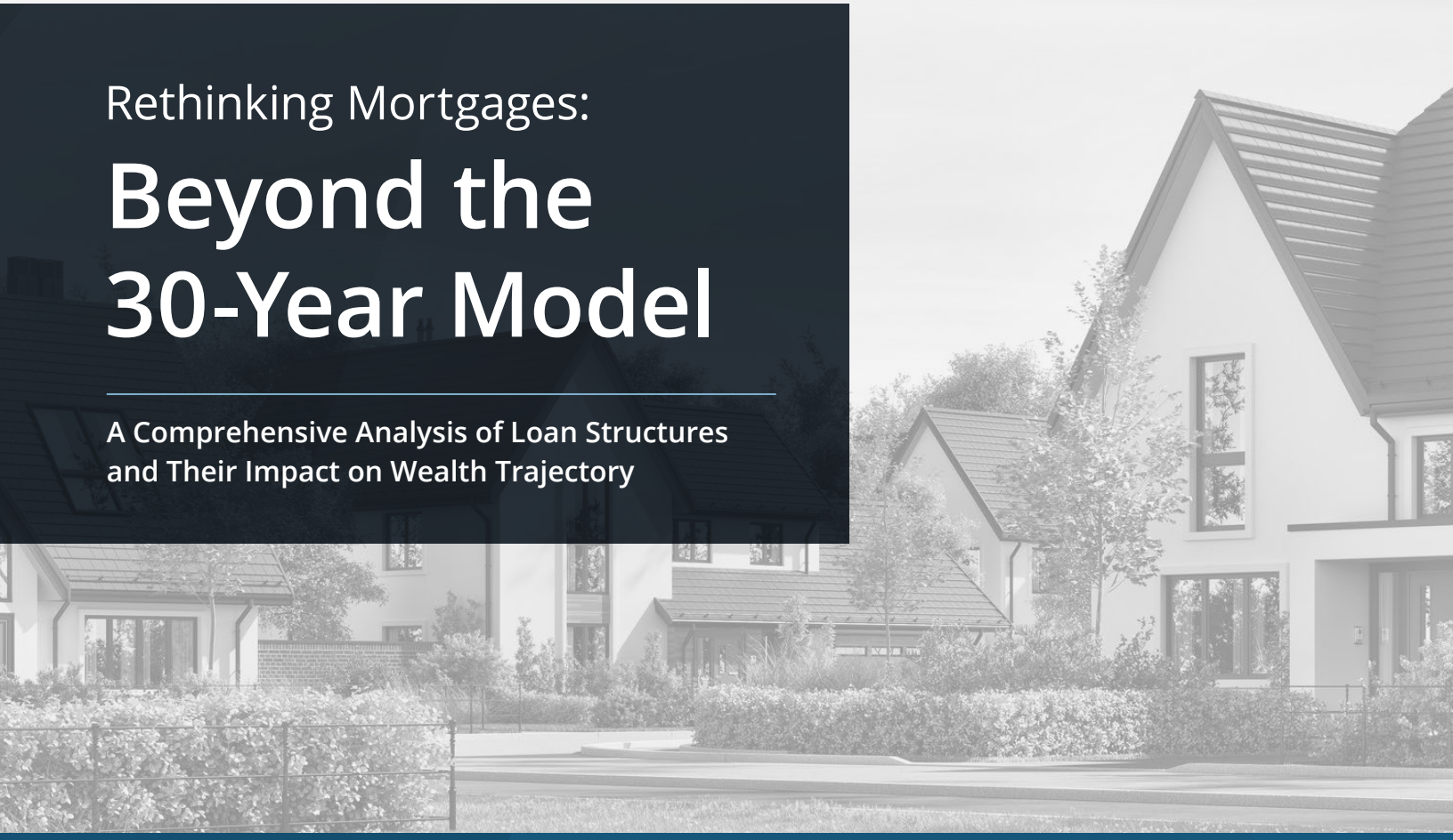


Rethinking Mortgages:

Beyond the 30-Year Model

A Comprehensive Analysis of Loan Structures and Their Impact on Wealth Trajectory

We are now deep into the 2020s. The world around us is very different from the one people navigated a century, or even just a few decades, ago. From trends in technology and culture to patterns of urbanization and homemaking and the rise of the digital revolution, we must constantly adapt to living, breathing, evolving environments. Change is the only constant. And yet, along the way, it seems as if the financing of the American Dream has become frozen in time.

Mortgage terms structured during The Great Depression are still commonly used today, almost a full century after they were developed. Could this be why homeowners collectively owe almost $14 trillion for their homes?[1] Might it also be a contributing factor to the growing retirement income security crisis?[2]

This whitepaper delves deeper into these questions, exploring the impact the traditional mortgage structure has on developing personal financial security and independence and potential modern solutions for a path forward.

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The Evolution of the Common Mortgage

Following the Great Depression, the landscape of homeownership changed significantly, primarily propelled by the establishment of the Federal Housing Administration (FHA) in 1934 to regulate mortgage terms. With a standardized banking system in place, the familiar forward-amortizing, closed-end mortgage emerged. The hopes? To reduce the risk to small borrowers, who previously had little collateral to leverage. Additionally, mortgages were now insured. Between this point and the 1970s, we see the development of three key government entities

- The Federal National Mortgage Association/ Fannie Mae
- The Government National Mortgage Association/ Ginnie Mae
- The Federal Home Loan Mortgage Corporation/ Freddie Mac

Post-World War II saw a surge in homeownership, driven by some public programs to expand housing access, like the Servicemen's Readjustment Act of 1944, or G.I. Bill.[3] Suburbanization accelerated, the single-family home became a viable reality, and the mortgage market flourished.

Here we see the traditional 30-year mortgage arise as we recognize it today. With the 30-year term, both demand and affordability accelerated, and price inflation served as an overall boon for both home construction and mortgage lenders. During this time, forward amortizing mortgage terms became widespread and led to increased affordability; eventually fostering the growth of the nation's middle class.

Key Features

The common mortgage structure that emerged from this period brought many perks to the table, namely:

Lower Down Payments: Before the conceptualization of a "true mortgage", loan terms were limited to forty or fifty percent of the property's market value, prohibiting most Americans from ever achieving homeownership. That changed with the formation of the FHA and the introduction of the forward mortgage, which allowed loan-to-value terms as high as seventy and eighty percent.

Achievable Payoffs: One of the hallmark features of the forward mortgage is its extended repayment terms, spanning as much as 30 years. This provided borrowers with a more affordable path to ownership compared to the 3 and 5-year balloon payment terms that had been standard. As the lending landscape took shape, these longer contracts also helped accommodate the rise in home prices.

Payment Stability: With the advent of the forward mortgage also came a fixed, amortized payment structure, offering borrowers the opportunity to reliably budget for their expenses without worrying about potential unplanned increases in interest rates or monthly payments. This helped those with mortgages keep their financial outlook more stable and predictable.

Together, these characteristics made the new forward mortgage an appealing option for home buyers during the postwar economic boom. However, looking at it from the mid-2020s, something else is clear: it was engineered for the times that created it.

The Evolution of the Modern Borrower

As we observe the financial environment evolve a century later, is this traditional mortgage still serving borrowers in the same way? Let's look more closely at how the modern borrower has evolved.

Transforming Needs

The mortgage landscape of the post-WWII Era was vastly different from today's ever more complex financial ecosystem. Back then, mortgages were designed to fit the needs of homeowners who were reasonably homogeneous in terms of financial status and stability. Fast forward to the 21st century, and the profile of the modern borrower has undergone significant transformation. This is driven by societal changes, economic shifts, technological advancements, and increased financial complexities.

Societal Changes

Since the 1930s, the demographics of borrowers have become significantly more diverse. Modern borrowers now come from a wider array of socio-economic and ethnic backgrounds, genders, and age groups. There has been a notable increase in single-person households, dual-income households, and older first-time homebuyers. Higher education levels among today's borrowers have influenced their financial literacy and decision-making processes. The traditional nuclear family model has also changed, with more single-parent households and cohabitating couples, leading to shifting borrowing patterns and housing needs.

Table 1	Then	Now
One person households	7.7%	29%
Average age of marriage	23 yrs.	29 yrs.
Average age starting family	23 yrs.	30 yrs.
Divorce rate	10%	50%

Economic Shifts

Modern borrowers face a far more volatile income environment compared to the (relatively) stable post 1930s job market. The rise of the gig economy, freelancing, and contract work models all contribute to fluctuating, unpredictable income.

Moreover, the increase in the cost of living has significantly out-paced wage growth, creating financial pressures that were less prevalent in the past. Today's borrowers often carry significant amounts of student loan debt, auto debt, credit card debt, and medical debt, which impacts their ability to qualify for and manage mortgages.

Table 2	Then	Now
Average annual income	$1,226	$74,580
Average price of home	$2,938	$420,800
Average price of home to average annual income	200%	560%

Technological Advancements

The advent of online banking, digital loan applications, and fintech innovations have revolutionized how borrowers access and manage their mortgages. The widespread availability of financial data and tools has empowered many borrowers to make more informed decisions. Additionally, the shift towards remote work (accelerated by the COVID-19 pandemic) has significantly changed housing preferences, with many borrowers now seeking homes in lower-cost-of-living suburban or rural areas rather than urban centers.

Economic and Financial Complexities

Modern borrowers have access to a wider array of investment opportunities, including stocks, bonds, mutual funds and real estate investment trusts (REITs). This diversification can also influence their approach to homeownership and mortgage choices. The mortgage market itself now offers a variety of complex loan products, from adjustable-rate mortgages (ARMs) to interest-only loans and reverse mortgages. Navigating these expanded options requires borrowers to have a deeper understanding of their choices and the associated risks (i.e., much improved financial literacy).

Table 3	Then	Now
Average household savings needed to retire securely	$123,400	$1,460,000
Percent of workforce with workplace pensions	60%	23%

Homeowner Mobility

Increased mobility is another defining characteristic of the modern borrower. Today's homeowners are more likely to relocated for job opportunities or lifestyle changes, necessitating greater flexibility in mortgage terms and structures. Refinancing has become a key tool for managing these financial situations.

Table 4	Then	Now
Average time workers remained at their job	10-21 yrs.	2.6-4.1 yrs.
Average number of years a homeowner keeps their home	12+ yrs.	8 yrs.

The Hidden Risk of Common Mortgages

This brings us to today, where social and economic factors, combined with the underlying structure foundational to the common forward amortizing mortgage, often lead Americans to replace their home loans long before they mature. This approach incentivizes buyers to leverage as minimal a down payment as possible to acquire real estate, commit the least amount of dollars towards principal, and then rely on market appreciation to increase their equity position. This can work—where favorable seller conditions and interest rates are available. Yet, the housing crash of the late 2000s shows how quickly that can go wrong.

It also draws attention to how many of the key benefits of a traditional mortgage, including payoff, are never actually realized. There's a good chance borrowers will refinance again or sell their home in the next 6.25 years[4] or less. Between 1994 and the first quarter of 2020, the median number of years a borrower kept a mortgage before refinancing was 3.6 years, according to recent data from Freddie Mac.

Table 5	Statistic
Percent of 30-year term mortgages	89%
Average lifespan of a mortgage	6.25 yrs.
Historical mortgage default rate	5.25%
Total U.S. mortgage indebtedness	$13.99 Trillion

Disincentive Structure

Four key factors, which we examine below, combine to disincentivize the modern borrower to commit more money towards principal. Instead of encouraging the mortgage holder to see their loan as a part of their wider financial planning and wealth accumulation, it becomes treated as more of an "inevitable monthly expense" that is continuously paid without ever building real capital for the holder.

It's easy to understand how this has happened. Until recently, there were few, if any, alternative mortgage products that reduced interest costs and monthly payments without relying on lower interest rates and refinancing or required change in budget. For those deciding whether to pay down the mortgage or invest, the argument is simple. Why tie up money in your mortgage when you can manage your monthly payment flow and allocate funds elsewhere? This is especially true when reducing the principal does not lower the monthly payment.

1. **Low Utilization of Income:** A relatively small portion of borrower resources are applied towards traditional amortized mortgage payments compared to the total amount of income earned on a regular monthly basis.
2. **Interest-First Payments:** Typically, 50% to 90% of traditional amortized mortgage payments is consumed by interest cost in the first ten years of a 30-year term loan, even with Pandemic-Era interest rates (see examples below).

Example 1

Number of Payments	30-Year Fixed Rate 6.000% Mortgage with a Starting Balance of $400,000				
	Total Payments	Total Principal	Total Interest	Percent Interest	Loan Balance
5 Years of Payments	$143,892	$27,783	$116,109	80.69%	$372,217
10 Years of Payments	$287,785	$65,258	$222,527	77.32%	$334,743

Example 2

Number of Payments	30-Year Fixed Rate 3.000% Mortgage with a Starting Balance of $400,000				
	Total Payments	Total Principal	Total Interest	Percent Interest	Loan Balance
5 Years of Payments	$101,185	$44,375	$56,810	56.14%	$355,625
10 Years of Payments	$202,370	$95,921	$106,449	52.60%	$304,079

3. **Non-Automatic Payment Recast:** Traditional amortized mortgage contracts with a fixed payment determine the interest cost and payment amount up-front, prior to closing per the amortization schedule. As principal is repaid and the outstanding loan balance lowers, the monthly payment obligation does not. If borrowers pay extra towards principal to lower their outstanding balance to save time, again, their payment obligation remains the same. This structure causes borrowers to refinance routinely to achieve greater monthly affordability.

4. **Closed-Ended Credit:** One of the hallmark features of the traditional amortized mortgage is its one-way payment system. Borrowers can only apply money into their loan and cannot take any of it back out. This makes paying more than the minimum monthly payment risky as money gets locked away permanently in mortgage prison.

One-Size Does Not Fit All

Nearly nine out of ten home loans sold have 30-year amortizing terms. While they can be a good starting point for new borrowers focused on establishing strong repayment habits, their structure can also delay the development of long-term financial security in ways that are often overlooked. Additionally, this one-size-fits-all approach may not be suitable for every stage of a homeowner's life. The advantage of a traditional amortized mortgage is reduced substantially as borrower's age, especially those nearing retirement. The low utilization of income, front-loaded interest, non-recasting payments, and lack of liquidity, can be significant drawbacks.

Personal Wealth Trajectory and Mortgages

While there is nothing inherently wrong with the 30-year mortgage model, it is arguably being misconstrued and 'misused' as a one-size-fits-all product that works for every consumer at every life stage. The perception of safety it brings has a real stranglehold on the market, with few thinking of their mortgage as anything other than a "thing they must have".

30-year mortgages represent over 89% of the current mortgage market[5], despite the limitations outlined above. The only other type that comes close is 15-year mortgages, at nearly 10%[6]. There is a failure to truly grapple with whether it makes sense given the individual's life circumstances and long-term financial wellness goals. Especially in a significantly changed economic environment.

Retirement is a Retreating Goal

The 30-year mortgage was tailored to a buyer facing a steady, predictable, full-time work trajectory also equaling about three decades. Generally, people worked for a single employer, staying rooted in a single area. They would service their mortgage for their working lives and retire with a cozy source of equity paid off in their name. As any Financial Advisor working today is aware, this client profile is now a rare breed.

Today, according to data from Bankrate and Fidelity Investments[7], retirement readiness among Americans has declined significantly. 56% of Americans feel off-track for retirement and 37% feel "significantly behind" a realistic retirement timeline. A study published by the National Institute on Retirement Security in February 2024[8], 79% of Americans agree that there is a looming retirement crisis. A remarkable 55% of Americans believe a secure retirement is unachievable.

While many financial strategists blame Congress for not acting sooner to restructure retirement savings plans, few seem to be taking how Americans service their debt obligations into consideration, let alone, how long-term exposure to interest costs may add friction. Presently, an estimated $14 trillion in mortgage debt[9] is outstanding, 65% of which is owed by borrowers 44 years of age or higher[10]. A typical Generation–X household, the generation of borrowers who owe the most on their homes, has only about $40,000[11] in retirement savings.

Table 6	Share of Total Mortgage Debt Outstanding
Silent (born between 1928 and 1945)	4.8%
Baby Boomers (born between 1946 and 1964)	29%
Generation X (born between 1965 and 1980)	42%
Millennials (born between 1981 and 1996)	24.2%

It's not getting any easier. Younger generations are becoming indebted earlier[12], in high inflation environments, making a comfortable financial future less certain than ever. People's work cycles are no longer fixed, with part-time and gig work on the rise. Circumstances are highly individual[13], with no singular common consumer profile remaining. It's a vastly changed market.

Conventional Thinking

A critical issue in today's mortgage environment is the tendency to reset the 30-year mortgage term by refinancing routinely, in pursuit of a lower payment or access to equity money, or both. Unfortunately, this practice has become normalized and often results in higher total payments over time, less equity accumulation, and capital appreciation pushed further down the road. This approach can leave future generations saddled not with assets, but just more debt to contend with, eternally rolling over.

Case Study

This first case study examines a $400,000 30-year fixed-rate mortgage used to purchase a $500,000 home and contrasts the differences in cost and payoff timing if the borrower refinanced twice in ten years to improve their rate by 2.250%, versus keeping the original loan in place.

30-Yr Fixed Rate Mortgage	Month	Rate	Int. Cost After 5 Yrs.	Int. Cost After 30 Yrs.	Cumul. int. Cost	Total Yrs. Indebted
First Loan (Purchase)	0	7.250%	$138,717	$570,158	$570,158	30 Yrs.
Second Loan (Refinance)	61	6.500%	$120,471	$487,250	$625,967	35 Yrs.
Third Loan (Refinance)	121	5.000%	$87,165	$338,115	$597,303	40 Yrs.

By refinancing twice, once after 5 years and again after 10 years, the borrower may have improved their monthly payment, but added tens of thousands of dollars in interest cost and a decade in mortgage indebtedness to their financial profile. This could also delay saving for other major needs, such as retirement.

A Holistic Approach

Benefits of refinancing depends heavily on the borrower's overall financial position and timeline. If one is looking to further the goal of building transformational savings and homeownership, a key part of the picture is missing. One must consider all key elements of a mortgage and how they align with the borrower's future needs.

- **Remaining Loan Term:** Helps in planning for payoff and assessing the impact of any changes to the loan.
- **Cash Flow Analysis:** Ensures payments align with the income and expenses, maintaining financial stability.
- **Liquidity Needs:** Considering the borrower’s need for accessible funds can influence decisions on whether to pay down the mortgage principal or maintain higher liquidity.
- **Existing Financial Stability:** Assessing the borrower’s overall financial health, including savings, investments, and other debts, provides a clearer picture of their ability to manage mortgage payments.
- **Financial Goals:** Aligning the mortgage plan with long-term financial objectives, such as retirement savings, education funding, or other investment goals, is crucial.
- **Payoff Goals:** Determining the borrower’s desired timeline for paying off the mortgage can help tailor the loan structure to meet these objectives.
- **Refinancing Costs:** Evaluating the costs and benefits of refinancing helps in making informed decisions that could lead to interest savings or better loan terms.

A Glaring Reality

But even with a more comprehensive approach, the fact remains; traditional mortgages seem outdated. Is it time for more flexible, personalized financing terms that better accommodate individual circumstances to be developed?

The Quest for a Better Mortgage Model

Being one of the biggest financial obligations any borrower will commit to in their lifetime, the mortgage must be structured to create long-term wealth and near-term flexibility and savings opportunities, and not just provide manageable monthly payments. By focusing on the future and the tangible goal of property ownership, we can ensure that modern mortgages contribute positively to developing financial independence and security.

A Modernized Mortgage for The Modern-Day Borrower

To create a mortgage model that better meets the needs of modern borrowers, a structure engineered to lower the cost of borrowed money (cost of funds) without depending on lower interest rates or a change in household budget, should be the focus. *To achieve that, four key changes should be considered:*

1. **Higher Utilization of Income:** One of the most overlooked financial assets in every borrower's possession is their checking account and the volume of dollars that passes through it. A modernized mortgage might make use of these funds to lower mortgage principal prior to being spent. Afterall, the typical borrower will manage more money through their checking account in just 5 to 7 years than they owe on their mortgage.
2. **Principal-First Payments:** While the world continues to evolve with the constant pursuit of efficiency, a modernized mortgage might include a principal-first payment system to place both borrowers and lenders in a better financial position. Principal-first payments can accelerate mortgage pay off and home equity growth, as well as reduce interest cost even if interest rates rise.
3. **Automatic Payment Recast:** A modernized mortgage might include reducing mortgage payments by recalculating the minimum monthly payment obligation with the outstanding principal balance as it's repaid each month.
4. **Open-Ended Credit:** Consider the additional financial security that having access to home equity money without refinancing would bring to homeowners. A modernized mortgage might include this feature to not only help borrowers navigate challenging times, but also provide an incentive for them to assert greater control of their payoff timing to meet other financial objectives, such as retirement security without the risk of losing access to applied funds.

White Paper Conclusion

As we've shown throughout this white paper, the traditional forward-amortizing mortgage structure was created for an economic and societal landscape that no longer exists for most Americans today. From increased social mobility to tightening economic pressure on our wealth-building goals and the rise of the gig economy, today's homeowner looks very different from that of the past. Addressing the shifting financial landscape and the impact that the mortgage debt has on long-term real wealth seems long overdue. There's a pressing need for the industry and any fiduciary to think beyond tradition and explore new paths and products engineered to work better for the borrower. Addressing the gaps in a model designed in and for a bygone era, and ensuring clients have a greater understanding of how mortgage debt impacts long-term financial goals as well as their immediate needs, is the ideal place to start.

About CMG Financial Services, Inc.

CMG Financial Services, Inc. (CMG) was founded by Christopher M. George and is the parent holding company to CMG Securities, LLC and CMG Mortgage, Inc. (dba CMG Financial, dba CMG Home Loans). CMG Mortgage, Inc. is one of the largest private independent mortgage banking firms in the United States. Other partner companies that fall under the CMG Financial Services, Inc. umbrella include Home Mortgage Advisors, LLC, Evo Home Loans, LLC (dba EPiQ Lending), The Gibraltar Group Mortgage, LLC, Linked Home Loans, LLC, (dba HomeGuide Mortgage), Next Mortgage, LLC, Select Lending Services, LLC, and Vision Lending Services, LLC.

Known throughout the industry for its consumer advocacy and product innovation, CMG launched its revolutionaryAll In One Loan™ program in 2005, a first lien line of credit and integrated checking account, to help homeowners flexibly reduce their mortgage cost aggressively, and later HomeFund It™ that modernizes the down payment savings process to the 21st century. CMG continues to challenge the status quo and transform the conventional lending landscape, promoting financial strategies that enhance long-term financial health and readiness.

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