What Do Interest Rates Mean?

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As you start shopping for a home loan, your first question of each lender will probably be "What's your interest rate? How much are you charging?"

Interest rates are usually expressed as an annual percentage of the amount borrowed. If you borrowed $120,000 at 10% interest, you'd owe interest of $12,000 for the first year. With most mortgage plans you'd pay it at the rate of $1,000 a month. You would also send in something each month to reduce the principal debt you owe - and the next month you'd owe a bit less interest.

When your grandparents bought their home (putting at least half the purchase price down, by the way), their interest rate was probably around 4 or 5%. Rates stayed the same for years at a time. Then in the years following World War II, things became more turbulent. As economic changes speeded up, rates began to change several times a year. By the l980s, lenders were setting new rates on mortgage loans as often as once a week - and they still do today. When inflation hit a high in the '80s, some mortgage loans carried interest rates as high as 17% - and those who absolutely needed to buy, paid that much.

Rates dropped gradually through the 1990s, and by 1998 had reached their lowest rates in decades. Heading toward the millennium, home buyers appear to have the most favorable conditions for mortgage borrowing since their grandparents' days - and without 50% down payments either.