

How Good Are Consumers at Choosing the Most Appropriate Mortgage Type?

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The mortgage crisis of the last few years has raised the important question of whether or not consumers are making appropriate decisions when it comes to mortgage types. Specifically, do consumers know when to choose an adjustable rate mortgage versus a fixed rate mortgage? Further, does mortgage education help consumers make the correct decision? This study uses unique data in which consumers were randomly assigned to either receive information explaining the difference between these two major mortgage types or to not receive any mortgage information at all. Consumers were then given two distinct situations where one of these mortgage types was more appropriate than the other. Multinomial logistic regression is used to determine the odds of consumers making the correct decision in each of the situations. The results suggest that receiving mortgage information does indeed make a difference in consumers selecting the appropriate mortgage type but by a smaller factor than predicted. 23% of those who did not receive mortgage education information correctly chose the most appropriate mortgage for both scenarios while 36% correctly answered both after receiving the mortgage education information. At the mean values of other variables, the predicted probability of choosing the best mortgage type was 60.2% for those who received the mortgaged education information and 38.3% for those who did not, which represents a significant difference between the actual odds. This may imply that consumers already had a bias towards the appropriate mortgage type before the two situations were presented to them. Factors such as overall financial knowledge and the score on a Truth in Lending Act quiz are also important predictors of choosing the correct mortgage type. Not all consumers who were exposed to financial information made the correct decision which supports the continued use of mortgage counselors and or educational programs to further assist consumers in selection the best mortgage type for their situation.

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