Is It Time to Refinance?

Over time, mortgage rates fluctuate. Depending on where rates currently stand, now may or may not be a good time for homeowners to consider **refinancing** their mortgage. How can you determine whether it makes sense at any given point to refinance your mortgage?

In the past, if the current interest rate was 2% lower than the rate you were paying on your existing mortgage, it made sense to refinance. That general rule may still apply in some cases. However, even if the rate were less than 2% lower than your existing rate, refinancing may still be an appropriate choice.

In addition to taking advantage of favorable interest rates, you might want to seriously consider refinancing to do the following:

Move from an adjustable rate to a fixed rate mortgage. Many first-time homebuyers must go with an **adjustable rate mortgage (ARM)** because they do not qualify for a fixed rate loan. If this was true for you, perhaps the rate for your ARM is about to go up. If so, you may be able to “lock in” a lower rate by refinancing with a fixed rate mortgage.

Build equity at a faster rate. Perhaps you would like to pay off your mortgage in less than the traditional 30 years. A drop in interest rates may allow you to refinance your 30-year mortgage and replace it with a 20- or 15-year mortgage at a monthly payment that may be close to what you have been paying. This option may be especially attractive to homeowners who are nearing retirement and would like to pay off their mortgages before they retire.

Replace a jumbo mortgage with a conventional loan. In most states, any mortgage over $417,000 is considered a **jumbo mortgage** (that amount is higher in expensive housing markets, such as Alaska, Hawaii, the U.S. Virgin Islands, and much of California). Jumbo mortgages have higher interest rates than do conventional loans. The difference between the rate for a jumbo mortgage and a conventional mortgage depends on the current market price of risk: and it can be significant—usually between 0.25% and 0.5%. If you have a jumbo mortgage, you may be able to refinance and pay down enough to qualify for a conventional mortgage, to get the lowest possible interest rate.

Take advantage of a lower interest rate. The most common reason for refinancing is that the current interest rate is significantly lower than the rate you are paying on your existing fixed rate mortgage. You will also need to consider variables such as refinancing costs, points, and how long you plan to stay in your home. It is always wise to shop around to ensure you are getting the lowest rate possible and paying the lowest cost.

Eliminate private mortgage insurance (PMI). PMI, which is required by most lenders if your original down payment was less than 20%, is tacked on to your monthly payment. If the value of your home has increased since you bought it, you may be able to have the PMI removed just by having your house appraised. Or you can eliminate the PMI when you refinance if you have more than 20% **equity** in your home.

Tap into your home's equity. If you have other debt or are anticipating new expenses, such as college tuition bills, you may want to refinance for a larger mortgage at a lower interest rate and use the extra cash to pay off the debt or forthcoming tuition bills.

Deciding when to refinance depends on the current rates, your personal financial situation, and your plans for the future. You may want to do some number crunching in advance to determine how much rates would need to drop for refinancing to make sense for you. Then you will be ready to make your move.

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