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With Mortgages so Low, Does it Make Sense to Refinance?

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Ask the Experts: With mortgage rates so low, does it make sense to refinance?



Historically low mortgage interest rates have prompted many homeowners to think seriously about refinancing, but there's a lot you need to consider before filling out a loan application.

Start by determining why you want to refinance. Is it primarily to reduce your monthly payments? Do you want to shorten your loan term so that you can save interest and possibly pay off your mortgage earlier? Are you interested in refinancing from one type of mortgage to another (e.g., from an adjustable rate mortgage to a fixed-rate mortgage)? Establishing a goal will help you determine if

refinancing makes sense for you and which type of loan will best suit your needs.

Keep in mind that the low mortgage rates that are advertised aren't available to everyone. To get the best rate, you'll need to meet the lender's criteria. For example, you generally need to have an excellent credit score, stable income, and substantial equity in your home--e.g., 20% or more. The type and length of the loan will also affect the rate you receive--in general, the shorter the loan term, the lower the rate. Advertised mortgage rates sometimes also include points that you'll have to pay to obtain the lower rate--each point is equal to 1% of the mortgage amount. Because so much can affect the rate you receive, it's important to shop around and compare interest rates, loan terms, and costs to make sure you're getting the best deal.

Finally, you'll need to consider refinancing costs as well as the new interest rate you'll receive. Refinancing costs may include points, closing costs, and private mortgage insurance premiums (if any) that you'll have to pay when you take out the new loan. Will you be able to recoup these costs while you still own the home? To calculate this, divide your total refinancing costs by the monthly mortgage payment savings you'll realize by refinancing. The result indicates how many months you'll need to stay in the home to recoup your costs. If you don't plan to remain in your home long enough to recoup your costs, then refinancing may not be worthwhile, no matter how low your new interest rate is.