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When Should I Refinance My House?

Many homeowners start off in a mortgage home loan that is less than ideal. They may have had bad credit and were forced to accept a higher interest rate and fees. Or maybe they just decided to buy when market rates were peaking. Fortunately for these types of borrowers and others with pricey loans, there is a way to get into a new loan with better terms. It is called refinancing.

Refinancing means the creation of a new home mortgage loan that will completely pay off your first loan. Some homeowners will do this just to get into a mortgage with a lower interest rate. Others will take advantage of lower interest rates while also getting a loan large enough to pull some extra cash out for other financial needs. Some will refinance into a shorter term loan, like from a 30-year to a 15-year loan in order to save money overall on interest payments. If you are looking into getting into a better loan, how do you know when it makes sense to refinance?

First of all you should take a look at the market interest rate trends. Typically, it is a good idea to refinance if the going market interest rate is at least 3% lower than your current mortgage rate. Otherwise the costs of creating the new loan may not be worth the savings you would gain. This is only a general rule however, and you consider many other important factors in making your decision.

One key piece of information that will help you determine whether now is a good time is how long you plan to stay in your current home. Because refinancing your current loan will cost you in both closing costs and resetting interest payments, to make refinancing a smart option, you need to remain in your home long enough to make the interest rate savings worth the new costs. For example, let’s say that your refinance loan will cost you $2000 in closing costs and fees and you will save $100 a month on your mortgage payment. Divide your upfront cost by the monthly savings. The result in this example is 20 months. This will be your “break-even” period. Staying longer than 20 months will create real savings for you, staying for a shorter period will end up costing you more than you save.

Another deciding factor may be the type of mortgage loan that you currently have. For example, if you presently have an adjustable rate mortgage and your fixed rate period is almost up, now may be the best time to refinance in order to avoid the resetting interest rate and higher payments.

Lastly, take a look at the current state of your finances. A refinance loan is just like your original mortgage loan in that you will have to pay closing costs and fees. You should evaluate whether or not you have sufficient funds at this point to cover the upfront costs of the new loan.

Getting a refinance home loan can often be very helpful for getting better loan terms and rates or for cashing in on your home equity. There are lost of factors to consider, so make sure you do your research. If a refinance mortgage loan feels like a good fit for you at this point, talk with your trusted mortgage professional to get started.