

Mortgage Mania

With interest rates lower than ever, the rush to refinance is on. Now, which of those two dozen deals is right for you?

By Sarah Lorge Butler

Risk averse and staying forever

The majority of homeowners prefer the predictability of a fixed-rate mortgage. Believing they've found the home they're going to stay in until old age, they sleep better knowing exactly how much their mortgage bill will be each month. With rates so low, why not lock one in for life?

That was the thinking of Katherine Schnall, a 30-year-old mother of two who bought her home in 1998. For his own deal, Schnall is taking advantage of the low, 2.75% interest rate on a six-month ARM with a second mortgage, which he's using to access the equity in his home. As a cash-out refinance, Schnall says, the proceeds go into a couple of investment vehicles, MLPs (master limited partnerships) and REITs (real estate investment trusts), which are earning between eight and 12% on money that's not their own cash, but it was our equity," he says. The loan they chose is based on the Libor, and for a period of time they're required to pay back only the interest.

Fixed-raters who plan a long-term stay can also go a step further by paying a point or two (one point is 1% of the loan amount) to "buy down" the interest rate to a lower number. Borrowers, however, tend to shy away from buy-downs. Says Michael Lubell, a mortgage banker for the New York Mortgage Company, "I think the consumer needs to be open-minded. They say, 'Just give me zero points!' O.K., but for a point, I can get you three-eighths better in rate. You don't want to know about that? You should."

Why? Because in the long run the lower rate saves more than the price of the points. For example, payments for a \$200,000, 30-year loan at 6% are \$1,199 per month. Say paying two points (\$4,000) lowers the rate to 5.25%. If you tack the points onto the loan amount, the monthly payment on a \$204,000 loan would be \$1,127. The \$72 monthly savings pays for the points in about 4½ years. If you carried the loan for the full 30-year term, you would save \$21,900 in interest payments.

We're moving in five years

Even though fixed rates are enticingly low, anyone certain to be selling his house—or paying off his loan—sooner than later should look at an adjustable-rate mortgage. "Adjustables do have a place," says Nick Papaioannou, a mortgage consultant for Washington Mutual. "It's more of a niche product, but in a very low interest rate environment, it can be a good option."

You can choose a term that best fits your plans. Is your family growing? In-laws moving back in? Expecting a job transfer? "When you know you're not going to be in your house more than a few years, there's no reason to pay for 30 years of security in a fixed rate," says Steven Schnall, CEO of the New York Mortgage Company.

How low can we possibly go?

Hybrid ARM rates are certainly attractive, but they're not the lowest of the low. Some lenders offer one-year, six-month and one-month adjustables, and if you're willing to risk more frequent interest-rate changes, these mortgage deals may make your eyes pop. Recent quotes range from 3.25% for a one-year ARM down to below 3% for a one-month deal. Like the hybrids, interest rates for these loans are based on an index, such as the one-year Treasury bill or the Libor (the London Interbank Offered Rate), plus a margin, which is an amount set by the lender that remains fixed over the life of the loan. These short-term adjustable also have their uses, particularly for those who want to minimize their monthly payment but don't mind paying more if rates rise later on. "Maybe you just got out of a medical internship," Schnall says. "You know your income is going to rise dramatically. But right now, while your income is low, you want the lower payment. When it starts to adjust up, you'll be making more money, so it's not that risky."

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With rates tracking so low, a short-term ARM can free up a lot of money. While Schnall invested his, an equally compelling option is to use it to make faster headway against the principal. The savings from the lower rate can be used to pay down the principal, which helps reduce the loan amount. Paying down the principal helps reduce the loan amount, which helps reduce the loan amount. Paying down the principal helps reduce the loan amount, which helps reduce the loan amount. Paying down the principal helps reduce the loan amount, which helps reduce the loan amount.

Of course, if the Libor jumps, so will Schmerzler's payments. This isn't a loan for the faint of heart or for anyone who doesn't understand all its nuances. Lenders say the short-term adjustables are most popular with financially savvy clients who can afford to risk a rate rise. "I agonized, then I thought, Let me just analyze it," Schmerzler says. "The numbers tell you what decision to make. They tell you what decision to make. They tell you what decision to make."

Bank Or Broker?

YOU'VE DECIDED THAT REFINANCING MAKES SENSE, and you're ready to jump on one of the great interest rates currently available. So where should you go, straight to a single lender or to a mortgage broker who can pick from several?

The truth of the matter is that you may be able to get equally good deals from both, but your first call should be to your existing lender. If your loan meets certain standards, the lender might be able to make the process easier or cheaper with a "mortgage modification," which lets you keep the same loan but lowers the interest rate for a fee of less than \$1,000. Another alternative is a "streamline refinance," which is a new loan, but requires less paperwork and often less expense. Even if you can't take advantage of one of these options, your bank may be eager to keep you as a customer and could, for example, offer lower closing costs. Keep in mind, however, that in the long run a lower rate matters more.

Whatever your lender can do, it's still worth a call to a mortgage broker to make sure you're getting the most competitive deal. In fact, banks count on brokers as a sales channel and give them lower interest rates. "Banks know brokers are looking at 30, 40 or even 50 different lenders," says Michael Lubell, a mortgage banker with the New York Mortgage Company. "If they don't give me competitive rates, why would I ever push their product? When you go into a bank individually, you're dealing in a vacuum. Chase isn't going to tell you, 'Our rate is pretty good, but Citibank's is lower!' But I will!"—S.L.B.