



Three Ways Lower Mortgage Rates Can Work For You

Just when it looked as if mortgage rates couldn't fall any further, they did. Rates on 30-year fixed-rate mortgages (excluding jumbos) hit an average of 4.3% in September, and 4.125% in August, the lowest level since 1953, according to Freddie Mac, and are still hovering below 4.25%.

Fifteen-year rates are even more mouth-watering: 3.8%. Mind you, those are averages. The most creditworthy borrowers can do even better, snagging rates perhaps a quarter of a percentage point lower.

So what's in this for you? A lot, potentially. If you have a credit score of 720 or higher and at least 20% equity in your home, you might use these crazy-low rates to shorten your mortgage term, free up cash, or even add to your real estate holdings, for example.

Whatever you decide, don't wait too long. "The consensus is that rates will gradually move up in the new year," says Frank Nothaft, chief economist for Freddie Mac. Freddie projects that the average 30-year fixed will hit 5% by the end of 2011.

Get Mortgage-Free Relief Sooner. It's easy to see why more than a quarter of borrowers today are choosing a 15-year mortgage, according to analytics firm Core-Logic, up from about 9% in 2007. A 15-year lets you save in two ways: You get a rate that's about half a percentage point lower than that of a standard 30-year, plus you can save tens of thousands by retiring the loan in half the time.

Let's say you took out a \$270,000, 30-year mortgage at 5.9% when you bought your house in 2005. You're paying \$1,596 a month in principal and interest and now have a \$250,000 balance.

Let's further assume that you roll \$5,000 in refinancing costs into a new 15-year mortgage at 3.8% (so the loan is for \$255,000). Your new monthly payment will be a heftier \$1,860, but you'll save more than \$147,000 in interest over the life of the loan.

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What if you can't manage the bigger monthly bite? Refi to another 30-year and simply pay more in months when you're able to, assuming you're disciplined enough to actually follow through with that plan.

Given that few new mortgages carry prepayment penalties anymore, kicking in extra money shouldn't be a problem, says Keith Gumbinger, vice president of mortgage data tracker HSH Associates. Caveat: If you have only a few years left on your current mortgage, or you plan to move soon, a refi may not pay off. Calculate how long it will take to break even on your closing costs, up to three years is typical.

Improve Cash Flow. Freeing up cash may be your biggest priority right now. Maybe you're trying to replenish your emergency fund after being out of work, or you have lots of high-interest credit card debt to pay off. Maybe your twins got into Harvard, and you need to cover some of the tuition out of current income. Or maybe you see enough investment opportunities around that you want to lower your monthly payment and invest the difference.

In those cases, choose a 30-year loan. Using the previous example, if you refinance to a \$255,000 30-year at 4.4%, you'll lower your monthly payment from \$1,596 to \$1,277. True, you won't save nearly as much in interest as you would with a 15-year. But that's not so bad, says Matthew Keeling, a certified financial planner in Mashpee, Mass., as long as you do something smart with the extra \$319 a month you'll save.

Double Down on Real Estate. Do your retirement plans call for moving to a house near the beach or a cabin in the mountains? If you can afford another mortgage payment, you may want to start your search now, while rates are in your favor and prices are depressed. Ditto if you've been wanting to buy a second home or an investment property, says Jonathan Bergman, vice president of Palisades Hudson Financial Group in Scarsdale, N.Y.

Assuming you're buying the place as a true second home, lenders generally charge the same rate they would for a primary residence. But if you intend to rent the place out, even if just for a few years until you retire and you need rental income to qualify for the mortgage, it's considered an investment property.

And mortgage rates on investment properties are running about a half to a full percentage point higher. Still, the numbers are "pretty compelling," says Justin Krane, a certified financial planner in Los Angeles... □

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