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CFS Financial Roundtable

Questions to Ask Before You Refinance

Hello this is Stephen Cross, a Financial Consultant, with today's Financial Roundtable

You might not have noticed, but mortgage rates are at historic lows. Which means refinancing your mortgage might make sense. Refinancing can be a great way to save money, but it's not a sure thing.

So, before refinancing, let's look at a few things you might think about...

First, make sure you have some time. Refinancing your home is an important financial decision and process. Make sure you have the time to study the loan terms and documents. If you happen to be too busy with work and family, it may be in your best interests to wait until you have more time to deal with the details of the loan. You do not want to miss something in the fine print and fall prey to a bad loan.

Next, will you breakeven or come out ahead? You will need to stay in the home long enough to cover the costs of refinancing. Yes, it costs money to refinance, and there is no need to do it if you don't at least cover these costs. A simple way to calculate this breakeven point is take the "total" cost of refinancing and divide by the amount you are saving per month. For instance, if it costs your \$2,000 to refinance and you will save \$200 per month on the new mortgage payment, then your breakeven point is 10 months ($\$2,000/200$). So you don't really save money until the 11th month.

Next, are you rolling other debt into your new mortgage? It might sound like a good idea to pay off some of your other debts by refinancing them into your new mortgage. The problem with this is if you roll a car loan into a 30 year mortgage, you end up taking 30 years to pay off that car loan instead of the remaining 2 or 3 years that were left on it.

Next, will I qualify for the rate I need? Your new rate needs to be a better rate at the same terms or the same rate at better terms. If it's not, you don't come out ahead. For instance, compare 30 year rates to 30 year rates and 15 year rates to 15 year rates. A 15 year rate will yield a higher monthly payment but you will pay the house off in 15 years and not 30, lots of interest saved in those 15 years!!

Next, can you meet today's tighter lending standards? A few years ago, during the housing bubble, it was easier to qualify for a home loan with favorable terms. Not now. Many lenders will demand a higher credit score. And forget about those famous "no-doc" loans, or "liar loans". They will be asking for full financial documentation.

Lastly, make sure you are not going from a good loan to a bad loan. Be honest with yourself and make sure you understand this whole process. Most lenders and brokers are honest and ethical, but we've all heard sad stories about people getting hoodwinked or steered into a loan that is not what they thought or wanted. Don't go from a good loan to a bad loan! If you feel like you need some help, find a trusted friend or advisor, and take your time. Don't fall for a bait and switch, or have them change the terms of the loan at the last minute on the day of closing.

Yes, refinancing can be a great way to save money, improve your short-term cash flow, and increase your long-term net worth. But a bad refinance can do just the opposite.

I'm Stephen Cross and this has been the Financial Roundtable