

**Many people hear phenomenal interest rates advertised for purchases and refinancing. Then, it turns out to be false. Why is that? While complex, the explanation is worth the read.**

## **The low DOWN on what's UP with the RATES . . .**

Contributed by Shawn Lynch of Venture Bank

With the interest rates fluctuating wildly in recent months and with the credit markets tightening dramatically, most borrowers just aren't sure where the rates actually stand and what it takes to qualify for the best ones. We felt it was time to shed a little light on the subject.

First, you have to understand that as crazy as the financial markets are presently, interest rates are just as volatile; maybe even more so. The days are long gone when you could watch a few benchmark indicators and have a good idea what the rates were going to do in the short-term. Right now, base interest rates are hovering in a range between 4.875% and 5.375%, with some short-lived forays into the areas above or below this range. By and large, you can expect a price change either up or down at least once a day. Today, as I am writing this article, there have been two (for the worse), and the day isn't over yet.

What does this mean for you? Well, it means that if you are in the market for a new home purchase or a refinance of your current one and the rate is at a point that works for you, I suggest you lock it and forget about it. This has been my advice to my clients for years and I believe it's especially applicable in these trying times. Rates are at historic lows and it is a great time to be a buyer or to look at refinancing your current property to more favorable terms. However, just remember that the rate you're being quoted today might not be there tomorrow. Hence the idea of locking it in and taking the worry about rate fluctuations out of the equation.

With all that said, there are some twists and turns regarding interest rates that didn't exist 7 or 8 months ago on Conventional loans. Understand that once the lenders give a people loans, they run out of money to offer more loans. Because of this, they bundle a bunch of loans together and sell them to wholesale loan servicers in the open market to get more money to loan out. As mentioned in the opening paragraph, the credit markets where the loans are sold have tightened dramatically and, as a result, the appetite for bundled loans has slackened. This lack of demand has required lenders to offer better performing assets (highly qualified home loan bundles) for sale or compensate investors with higher rates of return (read that as higher interest rates) for riskier loan profiles. These are reached through new add-ons to the base rates I mentioned above. To keep it simple, if you want a rate at or below 5% then you'll need to have a FICO credit score above 740 and not withdraw any equity on an owner occupied refinance or a new purchase of a primary residence. When your FICO score goes below the 740 mark or you are taking cash out of your equity, then you may begin to experience add-ons to the base rate. These depend greatly on your Loan-to-Value or LTV. That is a ratio best described as the amount you owe on your home divided by what it is currently worth. With a LTV below 60%, you won't have any type of adds to the rate with a FICO score at or above 660. But as your LTV increases, the add-ons to the points or rate can be significant. To illustrate, let's take a look at an example or two.

### Example Number 1:

Joe Schmoie and his wife, Martha, have a house with a mortgage of \$250,000 at a rate of 6.5%. Currently, it's worth \$334,000, giving them a 75% LTV (\$250,000 divided by \$334,000). They both have good credit, FICO's above 740, and they simply wish to lower their payments by refinancing. This case will qualify for our best interest rate because they have a FICO score over 740 and they do not wish to draw out any of their equity. This is called a rate and term refinance or a limited-cashout refinance (because the borrower is "limited" to a maximum of 1% of the loan amount or \$2000 of cash back at closing).

### Example Number 2:

John and Jane Doe have a house with a 1<sup>st</sup> mortgage of 150,000 at a rate of 7% and a 2<sup>nd</sup> mortgage (10 months old) used to consolidate debt for \$35,000 at a rate of 10%. The house is worth \$231,500 (LTV at 80%) and their mid-credit score is 640. This loan will be looking at a much higher rate. With the add-ons for the FICO score and cashout, this rate would be 6.50% or so today.

From the examples given, I think you can see that rates will vary greatly between two loans that appear to be quite similar. It's going to be hard to tell what your rate will be until you call your loan professional. That's the bad news on conventional loans.

However, there is good news and it comes in the form of government loans. FHA and VA loans are much less confusing. They don't have a lot of the add-ons that conventional loans do as long as the mid FICO score is at or above 620. Further, they offer streamline refinances for those individuals that currently have a government loan and are refinancing for the sole purpose of lowering their payment. These are very easy to complete and in many cases you don't even need to re-qualify; meaning that if you've lost a job or had hours cut back, you can still qualify for these types of refinances in many cases. Rates on government loans are very competitive with Conventional loans and in many cases offer advantages you just can't get with conventional financing these days.

The best advice I can give anyone is never assume that you're not going to qualify to buy a new home or refinance. Even with all the bad news in the headlines today, it really is a great time to be a buyer or to refinance your current home. Feel free to contact any one of the Residential Professionals Team (R-Pro) or myself to talk these issues over. You might just be pleasantly surprised.