

The Smart Homeowner's Guide to Refinancing



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Community Bank

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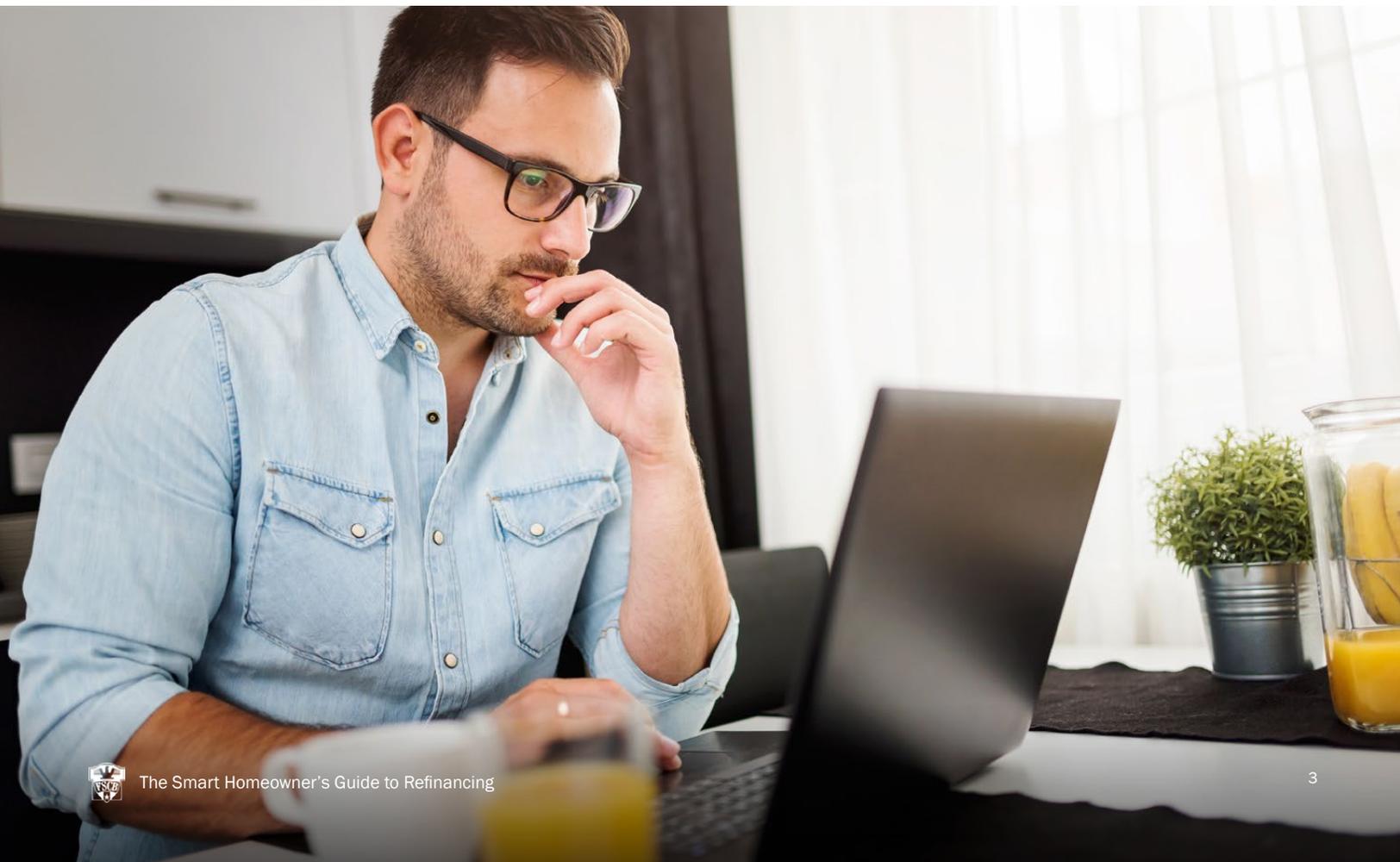


Introduction

Mortgage refinancing lets you access your home's equity and use it to further other financial goals or to address other urgent financial needs.

But before you dive into a refinance, it is important to understand all of the financial implications that come with refinancing, including the process itself, the types of refinancing available, the potential costs and rewards, and how to decide whether refinancing is right for you.

In this guide, we'll tell you everything you need to know to approach refinancing with confidence and financial savvy.



What Is Refinancing?

When you refinance a mortgage, you're taking out a new mortgage to achieve one or more financial goals by changing your mortgage terms and/or [tapping into your home's equity](#).

In most cases, consumers only seek out refinancing when they've built up equity in their home, although some homeowners seek out a refinance to take advantage of lower interest rates and/or to change other terms of their existing mortgage. Some borrowers will also seek out a refinance as a way to consolidate debt, using equity from their home to pay off credit cards and other high-interest debt and replacing those balances with a larger mortgage balance, which charges a much lower interest rate.

Refinancing might sound similar to taking out a home equity loan or opening a home equity line of credit (HELOC). But there are important differences between these products that homeowners should understand. Home equity loans and HELOCs use your home's equity to provide you with access to credit or cash, but they don't affect your existing mortgage.

A refinance replaces your current mortgage with a new one. The exact type of refinance you choose depends on your specific goals as well as whether you qualify for certain home loan programs.



What Kind of Refinance Are You Seeking?

There are a few main types of mortgage refinancing to consider, and they each offer different benefits and features depending on your goals when conducting a refinance. Here is a look at each type of refinancing, along with their benefits to borrowers.



Cash-Out Refinance

With a cash-out refinance, you increase the total amount owed on your home by taking out a mortgage that is larger than your previous one. The difference in that mortgage amount is then provided to you in cash, and you can use that cash however you would like.¹

Typically, homeowners use a cash-out finance to cover [home repairs or renovations](#), such as finishing a basement or replacing your home's windows. It could also be used to fund investment accounts, open a small business, or pay for college. Bear in mind that you should avoid using a mortgage to pay off debts, such as credit card balances and student loans. Replacing one debt with another doesn't offer a great financial return, and it can trap you even deeper in a cycle of debt.

Borrowers can also consider a limited cash-out refinance, which folds the costs of refinancing into the new loan and allows for a small amount to be taken out as cash. For this type of refinance, the maximum cash-out amount is the lesser of 2 percent of the loan or \$2,000.





Traditional Refinance

Also known as a “rate-and-term” refinance, a traditional refinance replaces your current mortgage with a new one that offers a lower interest rate and/or improved terms. Borrowers use this to reduce their interest rate and overall interest paid when rates are low and to lower their monthly payments.

You may also use a refinance to change the length of the mortgage. If you want to lower your monthly payment, you may refinance to extend the timeline for repayment. Or, if you want to build equity faster, you may opt for a shorter term that features a lower interest rate and accelerated repayment.

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Streamline Refinance

A streamline refinance is a simplified process that requires less documentation and underwriting than other refinanced mortgages. But a streamline refinance isn't available for every type of home or every kind of borrower. Streamlines are only available for government-backed mortgages, such as VA, FHA, and USDA loans. If you don't have one of those mortgages, a streamline refinance isn't an option.

Why Should You Consider a Refinance?

Refinancing shouldn't be taken lightly. It is an expensive process that only offers a financial benefit if you have a sound plan for how you'll recover those costs post-refinance. For refinances aimed solely at securing a lower interest rate, lenders argue that you need to reduce your rate by at least 1 percent to recoup the costs of refinancing through your interest saved. Some experts insist that the rate savings should be even greater—as much as 2 percent—to save you money in the long run.²

Additionally, refinancing isn't a resource you can keep coming back to—when you secure a new low interest rate, it could be years before you see better rates, if ever. And when you take equity out of your home, you're on the hook to pay it back—and it will take time to create more equity that you can borrow against.

However, there are times where refinancing offers a lot of value. Common uses of refinancing include:

- **Lowering your monthly mortgage payment.** If you're looking to lower monthly costs and make your home payments more manageable, refinancing can help spread out your repayment even further over time.

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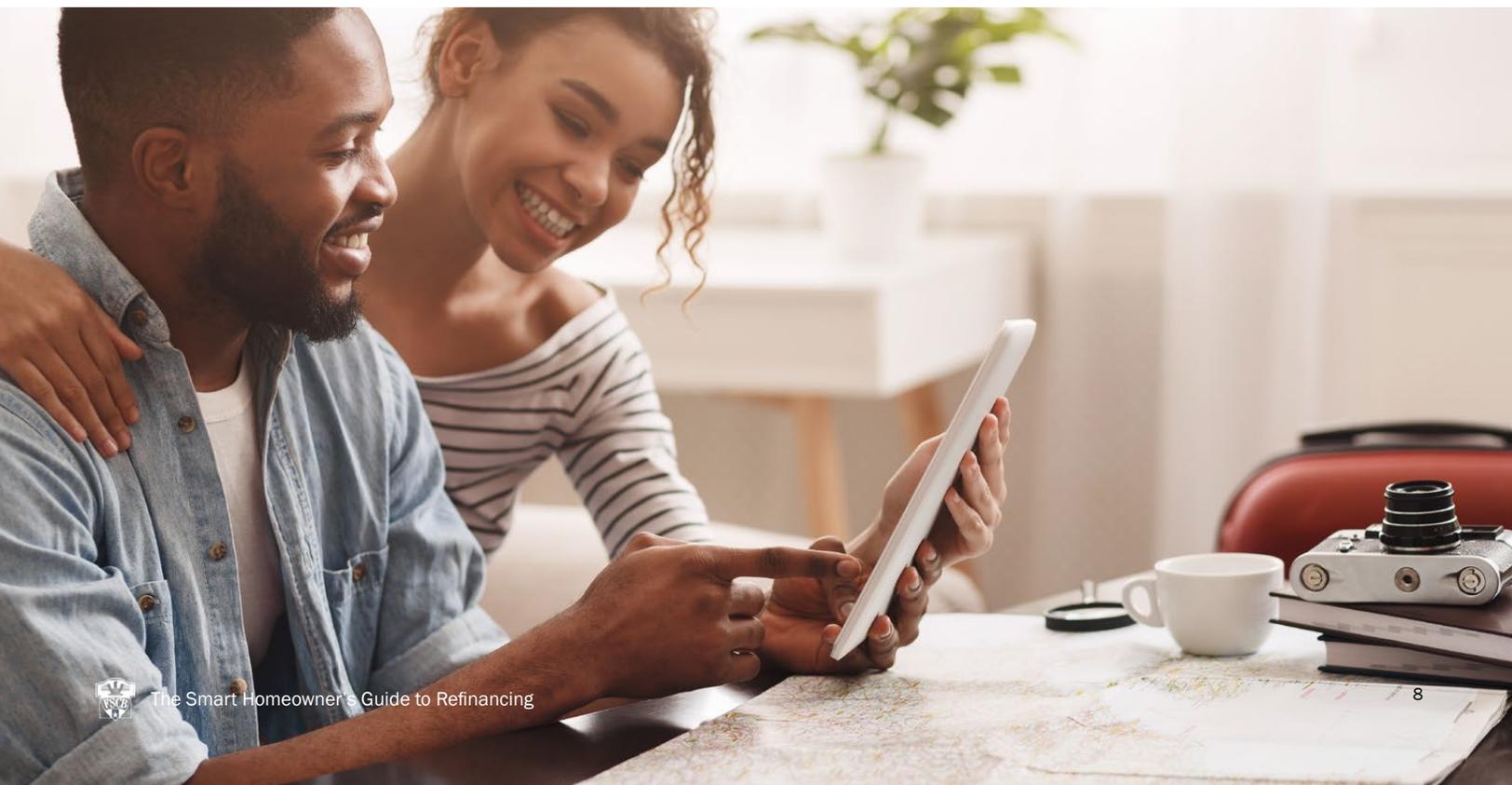


- **Taking out cash to pay for other expenses.** Homeowners use their equity to cover all kinds of big expenses and purchases, such as making home improvements and paying for college.

The key to this strategy is using equity as a way to avoid taking on more debt and at a higher rate than what you are paying for a mortgage. The rate on your refinanced mortgage, for example, could be significantly lower than the rate you would be paying for student loans, which offers long-term interest savings.

- **Switching your mortgage company.** If you're unhappy with your current mortgage servicer, refinancing can help you escape. Keep in mind, though, that many mortgages are sold after they've been originated, so the company you refinance with may not be the one that manages your mortgage.

If you're worried about your mortgage being sold after it is finalized, ask prospective lenders about their practice of selling mortgages to third parties before you start the refinance process.





- **Changing the type of mortgage on your home.** Do you want to switch from a 30-year mortgage to a 15-year plan? Refinancing can make that happen. The same goes for switching from a variable interest rate to a fixed interest rate on your mortgage—when you refinance, you can choose brand-new terms to suit your preferences.
- **Ending payments on private mortgage insurance (PMI).** If you put down less than 20 percent as a down payment on a home, you have to take out private mortgage insurance (PMI) to protect the lender in case you default on your home loan. Once your mortgage is valued at less than 80 percent of the home’s appraised value, though, you can get rid of PMI and lower your monthly payment.³

Refinancing isn’t always necessary to do this, but given that you’re already paying for a home appraisal, it can be a good time to consider whether refinancing is right for you.

Tips to Consider When Refinancing Your Home

Want to take advantage of refinancing for everything it's worth—and avoid costly mistakes at the same time? Here are some helpful tips to keep in mind:



Polish up your credit score before you apply to refinance. Refinancing is the same mortgage process you've been through before, and your financial background is going to be thoroughly vetted. That includes your credit score. Take steps before refinancing to get your credit score in the best shape possible: Keep debt utilization low, continue making on-time payments, and don't close any accounts or open new lines of credit when you know you're about to refinance your home.



Be ready to jump on lower interest rates. Drops in interest rates can come without warning. These opportunities don't last forever, so if you've been wanting to refinance and rates are low, don't hesitate. If you do, it could cost you some percentage points.

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Pay attention to home valuations in your area. Making payments builds equity in your home, but so does rising demand in your neighborhood. If your neighbors are selling their homes at a huge profit, it could mean you have equity in your home that could be better applied to other financial goals.



If you're cashing out, figure out how much you need. It can be tempting to take out whatever you qualify for, but that's a risky financial move if the funds aren't managed properly. Have a concrete plan for what you'll do with any equity you cash out.⁴



Clean and tidy your home before the appraisal. Your home appraisal ultimately determines how much equity you're able to cash out, and it determines whether you're able to get rid of PMI. Make sure your home is spotless and well-furnished to maximize your appraised value.

As you prepare to refinance, think of the process as a job interview: You want to put your best foot forward. A little preparation and fine-tuning of your finances could affect the interest rate you receive or even whether you're able to qualify for a refinance at all.



How to Start the Refinance Process

To start the refinance process, you'll want to meet with or [contact a trusted lender](#) to discuss your needs and your refinancing goals. Then you should start an application and take the steps necessary to lock in a mortgage rate from that lender.

As the process goes on, find out the fees you will be charged, the appraised value of your home, and the total amount and terms of your proposed mortgage refinance.

Use a [mortgage refinance calculator](#) to make sure the long-term savings of this move outweigh the up-front costs. You can also use this calculator to verify that you're able to handle your new mortgage payment increase, if you expect an increase.

Like any other mortgage process, a refinance typically takes up to 45 days to complete. This time frame can be shorter depending on your specific circumstances and the readiness of your documents, but you should plan for 45 days when setting timelines for this process.

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Conclusion

Most homeowners refinance their mortgage at some point in their lives. Whether you're looking to improve your terms, cash out money, dump PMI, or all of the above, approach refinancing with a clear sense of your financial goals, and find a trusted lending partner to guide you through this process.

Most homeowners refinance their mortgage at some point in their lives.

Looking for a lender to assist you in your home refinance? Visit your nearest First State Community Bank branch today.

[Get in Touch](#)



Key Refinancing Terms

Amortization Schedule

An amortization schedule details each scheduled payment on your mortgage for the duration of the loan. This schedule also breaks down the amount of principal and interest you will pay with each payment.

Adjustable Rate Mortgage (ARM)

An ARM offers a fixed interest rate on your mortgage for a set period of time, followed by a period during which the rate is automatically adjusted according to the lender's variable base rate. This will cause your interest paid and your monthly mortgage payment amount to vary over time after the fixed period is over.

Closing Costs

The expenses you will be charged when financing or refinancing a mortgage. Closing costs can include lender fees, attorney fees, title insurance, and taxes, among other costs. Some of these fees may be negotiable with your lender.

Down Payment

The amount of money paid in cash to purchase a home. A down payment represents the sale price of the home not covered by the mortgage.

Interest Rate

The amount you will be charged on your mortgage. This can be a fixed rate or an adjustable rate that varies over time (see Adjustable Rate Mortgage).



Equity

The value of a home that exceeds what a homeowner owes on their mortgage. If you owe \$250,000 on a home worth \$315,000, your amount of equity is \$65,000.

Origination Fee

A fee charged by mortgage lenders at the start of a loan agreement to cover the cost of loan processing.

Principal

The amount owed on a mortgage, excluding interest.

Private Mortgage Insurance (PMI)

An insurance policy used to protect the lender if they are unable to pay for the loan. PMI is typically required when the mortgage on your home is greater than 80 percent of the value of the home.

Term

The established time frame over which the mortgage will be paid. Typical mortgage terms range from 15-30 years.

Sources

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About First State Community Bank

Since 1954, First State Community Bank has been a leading financial resource to residents and businesses across the State of Missouri. First State Community Bank has built its reputation on an unyielding commitment to delivering the best possible service to customers and partners, from the Junior Savers who open an account with \$1 to those applying for multimillion-dollar commercial loans. Our mission is to help our customers achieve financial success on their terms, whether that means buying a new home, starting a business, or planning for retirement. We are here to help you reach your financial goals today and into the future.

Ready to start fresh with a better bank?

Connect with the FSCB team to find out how to make the switch.

[Get in Touch](#)

