"Everything in the heavens and earth is Yours, O Lord, and this is Your kingdom. We adore you as being in control of everything. Riches and honor come from You alone, and Your are the Ruler of all mankind; ... "
— I Chronicles 29:11-12

Rate is not the # 1 consideration in a mortgage loan

By Dale Vermillion

During the week of January 9th, mortgage rates hit the lowest level recorded since the Mortgage Bankers Association survey began in 1990 (4.98%). And although interest rates have increased about one-half percent since then, there are still great rates available on mortgage loans today (see **www.bankrate.com** for the latest rates). In these times of economic uncertainty, this is great news if you are a homeowner who is thinking of refinancing. However, let me tell you something that you may have never been told before – *the interest rate is NOT the most important consideration on a mortgage loan!*

That's right! All we have ever been told is that *rate matters!* We have been programmed that *rate is the primary consideration* when borrowing—nothing is more important. The truth is, when finding a mortgage loan that has true financial value and makes good overall financial sense, the interest rate, *although important*, is only one of numerous criteria to consider (others being equally or more important to the overall cost and benefits of the loan). These factors include the loan term, the tax implications, the fees and the overall savings, among other things.

In my book, *Navigating the Mortgage Maze: the Simple Truth About Financing Your Home (Northfield / Moody Publishing, January, 2009)*, I open with the ***Top 10 Mortgage Traps***. The first of these is ***Making Rate the #1 Consideration -*** this is a common mistake that can cost us tens of thousands of dollars needlessly!

Ephesians 5:15-17: tells us, "*So be careful how you live. Don't live like fools, but like those who are wise. Make the most of every opportunity in these evil days. Don't act thoughtlessly, but understand what the Lord wants you to do (NLT)."* God does not want us to have financial burdens. He knows that we cannot be all He intended us to be if we are burdened with debt we cannot afford. Jesus told us in His sermon on the mount *(Matthew 6:24)* that *"No one can serve two masters. Either he will hate the one and **love** the other, or he will be devoted to the one and despise the other. You cannot serve both **God** and **Money."*** Therefore, if we can refinance our mortgage today and improve our overall financial picture, we are following His direction. To do this we must consider more than just the interest rate, because it does not ensure a better financial picture. Let me prove this by using a scenario from my book:

> *The Brunsons bought their home in the eighties when interest rates were high. They started with a 10 percent, thirty-year mortgage. Every time rates dropped, they refinanced. They just completed their eighth refinance and are down to a 5.0 percent interest rate, lower than any rate in the market! The Brunsons feel they have managed their mortgage very well and have saved themselves tens of thousands of dollars in payments over the years through the many rate reductions.*
>
> *Unfortunately, the Brunsons have actually lost hundreds of thousands of dollars without even knowing it. You see, although they have reduced their rate eight times, they have also extended their term eight*

> *times, paid fees eight times, and decreased their taxes eight times! The result: they have been paying for twenty-four years on their home, owe more today than they have ever owed, and are no closer to being debt free . . . and retirement is twenty-four years closer than when they got their first mortgage! Although the Brunsons have the lowest rate they have ever had, they are in the worst position they have ever been!*

Does the Brunsons' story sound familiar to you? Have you made this same mistake? What the Brunsons have done is what I refer to as "the perpetual refinance." This is very common. For many of us, it feels like the only thing besides heaven that is eternal is our mortgage payments (thank the Lord that we know better)! Let's focus on the first factor to consider that is more important than the rate – *the Loan Term.*

The Loan Term

I believe the loan term is possibly the most important factor in mortgage financing. Why? Here are four reasons:

- **Debt Freedom is God's Plan for Us:** As Christians, our goal is to get out of debt as quickly as possible; debt is simply *"debt-trimental!"* The Bible gives us great instruction in Romans 13:8, "*Owe nothing to anyone—except for your obligation to love one another. If you love your neighbor, you will fulfill the requirements of God's law"* (NLT). Wouldn't that be a great life if our only debt was to love one another?

- **Term is the Biggest Factor in the Total Cost of the Loan:** Loan term affects the total cost of the loan more than the interest rate in most cases. The interest rate affects only one thing in a loan – *the monthly payment*. However the term affects *the total repayment*. Although the payment impacts the short term cost, the repayment affects the total cost. When looking at a mortgage loan, which is typically the largest financial transaction we make, it is critical to consider both!

- **The Term Impacts Your Future:** One of the key principles for borrowing that I cover in my book is establishing a *Debt Elimination Date,* or *DED* (and it is hopefully before we are dead!).Many of us go into a mortgage and do not think about the impact of the term or think we will either refinance, sell or pay extra each month to pay it off sooner. Before we know it we end up in our 50's and still have 20 or 30 years left to pay. At that point, being debt free seems impossible. We never want to plan our retirement without including debt freedom in that plan. Therefore, establishing an immovable target date to be debt free helps us to choose terms that keep us on the Biblical path of debt freedom.

- **The Shorter the Term, the Lower the Rate:** Finally, although rate is not THE most important factor, it is certainly one of the most important factors in choosing a mortgage loan. Because shorter term loans typically carry lower rates (because there is less risk to the lender), it just makes good "cents" to get a shorter term.

So why are the overwhelming majority of mortgage loans for 30 year terms? I believe there are two primary reasons for this: (1) because we think there are only two options – 30 years or 15, and (2) because we think the payment difference between the two is nearly double. Neither of these is true.

Odd Term Loans are Readily Available: Did you know that many lenders offer 25, 20 and 10 year terms along with their 30 and 15 year terms? That's right. They are actually very common. The beauty of a 25 or 20 year term is that there is very little difference in the monthly payments, yet a dramatic difference in the total repayment. Let me give you an example by comparing a 30, 25 and 20 year refinance for a $100,000 loan:

$100,000 at 5.25%	30 Year Refinance	25 Year Refinance	20 Year Refinance
Monthly Payment	$552.50	$599.25	$673.84
Payment Difference	N/A	$46.75	$121.34
Term Impact	N/A	(2 Years)	(7 Years)
Total Repayment	$198,793.33	$179,774.31	$161,722.60

Repayment Difference	N/A	$19,019.02	$37,070.73

A nominal *investment* of $46.75 (for the 25 year term) *guarantees* $19,019.02 in interest savings. The reason is the rate and term are both *fixed*, thereby assuring the return. In addition, the debt is paid five years sooner. For a 40 year-old borrower, this is the difference between being debt free at a retirement age of 65 or having to wait until 70. This could have a profound impact on your retirement plans, as most of us go from a normal income to a reduced, fixed income. It is hard to place a value on that!

Now you may be thinking:

- But I could take the 30 year loan and either pay the extra myself to payoff in 25 years, or;
- I could invest the $46.75 per month on my own to build a savings account, or;
- But I don't plan on being there for the full term, so aren't I better just saving the money now and getting a short term loan next time?

The answer to all of these is yes, you could. But the first question for any of these is will you? It takes a lot of discipline to do any of these things *every month* for 300 months. Many set out intending to do this, but then end up moving off that plan when things get tight. There's an old saying that applies here - "the road to good intentions can lead to ruin." Let me address the remainder of these questions individually:

- **Pay Down on My Own:** If we can pay the extra money each month to guarantee debt freedom sooner, why not just commit to it and ensure the savings? This is what I refer to in my book as creating a "forced savings account."

- **Invest on My Own:** As for investing the money, if you applied the $46.75 to a monthly account at the same 5.25% investment return, you would actually have more money at the end of the 25 years – a total of $29,389. However, where, in today's economy and investment market, can you get a fixed rate of return of 5.25%? Based on the $19,019.02 savings created through the term reduction, you average a guaranteed return of 2.25%. Third, depending on where you invested the money, you would have to pay taxes and end up with less savings overall. Through mortgage financing you actually gain a tax deduction. Fourth, investing would not help you pay your mortgage off sooner.

- **Payoff Sooner:** When you plan to pay off and when you want to be debt free is the answer. If you sold in five years, you would have paid $2,805 in additional payments for the 25 year loan, but only seen $1,387.50 in additional principal reduction to your loan. Therefore, it would cost you $1,417.50. But if you sold in 10 years, you would have spent $5,610 in additional payments but reduced $7,403.64 in additional principle. In this case, you would benefit by $1,793.64 (and this keeps growing each year). I lean towards *always* opting for shorter term because it put you on pace for guaranteed savings and term reduction.

If we have to borrow, particularly on a large and long-term transaction like a mortgage, we do not want to spend any more on interest than we have to. After all, it's God's money, not ours! He has entrusted it to us. The money we save can be used for purposes to honor Him and expand His Kingdom. Ephesians 1:22 says *"God has put **all things** under the authority of Christ and has made him head over **all things** for the benefit of the church"* (NLT).