New Mortgage Rate Record; What Is a "Top Tier" Scenario?

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Mortgage rates are on a tear, with the average lender easily hitting new all-time lows today. How low is that? At this point it's safe to say that anything over 3% is too high as long as we're talking about a top tier scenario. So let's take a moment to discuss what might separate one scenario from another.

1. Loan-to-Value ratio (LTV)

As the name implies, it's the ratio of the proposed new loan amount to the value of the home in question (note that the purchase price is used if it's lower than the appraised value). This one of the two most important considerations that determines the pricing bracket your loan quote would fall into. By the time you get an LTV down under 75%, you're paying almost no additional interest, but there's a very important caveat.

2. Credit Score (FICO)

This is the important caveat. If the middle of your 3 credit scores (as pulled by your mortgage lender) is over 740, then the conclusion above (about LTV < 75%) stands. Fall under 740, and loan costs will begin increasing steadily. Even with 25% down (aka 75LTV), there's a staggering difference between a 740 credit score and, say, 679. For example, someone with the lower score would pay an additional $6000 in closing costs assuming a $300k loan on a home worth $400k. Interestingly enough, if that person could find another $60k of equity (i.e. if they only needed a $240k loan on a $400k home), that $6000 would vanish completely.

3. Occupancy

This refers to whether you'll live in the home as your primary residence or rent it out. There is a small hit for a bonafide second home, so we'll focus on the investment property hit instead. On that same $300k loan, the difference between owner occupancy and investment property is roughly $6400 upfront. Unlike the credit score hit, this one wouldn't go away if you decrease the LTV. And if you can't make it down below 75 LTV, brace yourself. It'll be close to $10k at 80LTV and over $12k for anything above that. And this is BEFORE any adjustments for credit score.

4. Cash-Out

If you're not simply paying off purchase money loans during a refinance, you'll be hit with a cash-out adjustment. At our example 75LTV, this will cost you just under $2k assuming the 740+ credit score and $3k if you're between 700 and 740.

The aspects above are **the big 4** when it comes to determining loan pricing, although there are several other potential factors (condos, multi-unit homes, high balance adjustments, subordinate financing hits, etc). The point of diving into this is to add clarity to the notion of a "top tier scenario." Simply put, this would assume at least 25% equity (75 LTV), a 740+ FICO, no cash out in the event of a refi, and owner occupancy.

The current rate environment is very kind to those scenarios but relatively brutal for everything else. This is a normal byproduct of a big, sustained drop in rates. Even if we only change the credit score to 679 and leave everything else in its top tier position, the average lender would still need to raise your rate quote by .375-0.50% in order for your upfront closing costs to remain unchanged. Either that or you could simply opt to pay an additional 2.25% of your loan amount at the closing table.


8%
6%
4%
2%
0%
2016
2018
2020
2022
2024
30 Yr. Fixed
15 Yr. Fixed
30 Yr. FHA
30 Yr. Jumbo
5/1 Yr. ARM