



**RESEARCH BRIEF**  
Mortgage Refinancing

**SEPTEMBER 2021**





## STATE OF THE RESEARCH

Given historically low interest rates in 2020 and the first half of 2021, a number of households have refinanced mortgages to reduce their housing costs. Recently, a number of articles in the national press and publications from academic research centers have called attention to racial differences in those who are refinancing. While research suggests Black homeowners would realize greater savings than other racial groups through refinancing, they were only half as likely to have done so relative to white homeowners. Current research and commentary are seeking to spotlight these differences, identify the causes of the disparities, and suggest action that could be taken to resolve the racial gaps in refinancing.

## BACKGROUND

The interest charged on a home loan is bundled into a monthly mortgage payment, comprised of repayment on loan principal, interest, and any additional fees or services (such as private mortgage insurance) associated with the home loan. Interest rates for a particular borrower are influenced by several specific factors—including attributes of the borrower (e.g., a borrower's current income, assets, debts, credit score), terms of the loan, and other considerations—as well as more general economic factors. In the latter category, the current economic and fiscal environment can strongly influence mortgage interest rates; for much of 2020 and the first half of 2021, mortgage interest rates have been at record lows.

Record low interest rates reduce the cost of borrowing for homebuyers; although for new buyers, research suggests the price of housing may adjust upwardly when interest rates decline. Nevertheless, current homeowners may save thousands of dollars through reducing their current interest rate by refinancing their mortgages.

There are generally costs associated with refinancing a loan, and the decision to refinance may be influenced by several factors, including whether one plans to remain in their home long enough for the savings on mortgage payments to offset the closing costs associated with refinancing. Recent research from Freddie Mac found that, on average, homeowners who refinanced 30-year fixed-rate mortgages in 2020 saved more than \$2,800 annually and reduced their interest rate by a full percentage point.

However, recent research has identified racial differences in the borrowers taking advantage of current opportunities to refinance mortgages. A study from the Federal Reserve estimated that between the start of the pandemic through October 2020, the rate of refinancing for Black homeowners was half that of white homeowners (6 percent of Black homeowners versus nearly 12 percent of white homeowners). In addition to examining these differences and their impacts, researchers have sought to examine potential causes for the disparities as well.

## SUMMARY OF RESEARCH FINDINGS

Much of the recent research findings and commentary around this topic stem from a report by the Federal Reserve Banks of Boston, Atlanta, and Philadelphia, entitled “*Racial Differences in Mortgage Refinancing, Distress, and Housing Wealth Accumulation during COVID-19*”, and a brief released by Freddie Mac entitled “*Almost 50% of Black and Hispanic Borrowers Could Save \$1,200 Annually by Refinancing*”.

### *Observed Differences in Refinancing and its Impacts*

Black and Latinx homeowners pay higher interest rates, in general, than white homeowners; a *Money* magazine article from June 2021 cited research that found that between 2005 and 2015, Black and Latinx borrowers



paid, on average, mortgage interest rates that were 0.4 percentage points higher. One driver of that difference was that householders of color were less likely to refinance.

The Freddie Mac research report, referenced above, found that nearly 50 percent of Black and Latinx borrowers could expect to save at least \$100 a month by refinancing, or more than \$1,200 per year. Further, nearly 20 percent of Black and Latinx borrowers could expect to save at least as much as \$200 per month through refinancing. Expected savings from refinancing for Black and Latinx homeowners were higher than white homeowners at every threshold of savings examined.

While the potential savings for households of color are considerable, these households have been less likely to refinance in the current interest rate environment. The Federal Reserve report, referenced above, found that, given differences in Black and white homeownership rates, while a total of \$5.3 billion was saved by all households through refinancing between March and October 2020, only \$198 million (3.7 percent of the total) was realized by Black homeowners (Black homeowners represent 9.1 percent of all homeowners).

### *Challenges: Why aren't Black-led Households Refinancing as Frequently as White-led Households*

The two research pieces referenced above, by the Federal Reserve and Freddie Mac, have spawned additional commentary, much of which examines challenges faced by households of color in accessing refinancing. While some research focuses upon challenges that are short term in nature—stemming from specific challenges faced by Black families during the COVID-19 pandemic—others examine broader, more structural considerations.

In examining short-term considerations (while recognizing these considerations are based in broader structural issues), the *Money* magazine article cited above notes that job losses during the pandemic were disproportionately realized by workers of color; losing a job on its own could disqualify a borrower from refinancing due to income requirements.

More broadly, the disparate economic fallout from the pandemic led to more Black homeowners missing mortgage payments and/or entering forbearance. The Federal Reserve found that 12.3 percent of Black homeowners missed payments between January and October of 2020 while only 4.3 percent of white homeowners missed payments; among those that missed payments during that time, Black borrowers were less likely than their white counterparts to have “cured” their loans by resuming payments or paying off the loan. Due to federal legislation that allows for borrowers to seek a loan forbearance, missing payments during the COVID-19 disruption is unlikely to have the same impact to credit scores or foreclosure that may have occurred otherwise; nevertheless, loans in forbearance generally are not eligible for refinancing which limit the ability of groups to avail themselves of the potential savings.

In addition to disruptions attributable to the pandemic, due to wealth disparities between Black and white households, research suggests that households of color may have greater difficulty in paying the closing costs associated with refinancing. Freddie Mac estimates that the average closing costs associated with refinancing are around \$5,000. According to a recent survey conducted by the Federal Reserve, 59 percent of Latinx borrowers and 53 percent of Black borrowers (compared with 32 percent of white borrowers) had less than \$5,000 in liquid assets. Thus, these liquidity-constrained households are, in effect, “locked out” from realizing the savings associated with refinancing.

Research also suggests that the high demand for refinancing among a somewhat tighter than usual mortgage market has constrained access to refinancing options for households of color. With households of color having, on average, lower credit scores and higher loan-to-value ratios, many households were less able to access



refinancing options relative to households that were more favorably positioned—in terms of their assets—to do so. These concerns may be further exacerbated by potential appraisal bias—when appraisers value homes in neighborhoods of color or homes owned by persons of color lower than similar houses elsewhere; when appraisals for homes are low, the loan-to-value ratio appears riskier for lenders, thereby reducing the likelihood of a particular applicant in receiving the loan.

In addition to the quantifiable issues outlined above, it may be difficult to assess the degree to which a lack of trust between communities of color and traditional mortgage financiers reduces the likelihood that a household of color will seek and pursue refinancing. A Wharton School associate professor of real estate and finance, Benjamin Keys, notes the wariness that many households of color have regarding the country's housing and banking infrastructure. Specifically, he cites many borrowers of color having difficult experiences in qualifying for their original mortgages, leading them to be less likely to engage in a similar process for refinancing.

### **Potential Solutions**

Given that broad attention to racial differences in refinancing is relatively recent, research on potential solutions is relatively limited at this time. Nevertheless, Mr. Keys – citing a 2015 study by researchers from MIT and Emory University, within the *Money* article—noted that a peer's positive experience can trigger a cascading effect after which others will pursue refinancing: "Some borrowers may stay on the sidelines until they've heard from a trustworthy source that it's a good time to refinance." Mr. Keys also notes that individuals who had a positive experience with a lending institution are more likely to refinance.

Beyond working to resolve trust issues, researchers noted the potential for lenders to examine zero closing costs and reduced verification requirements to facilitate refinancing among borrowers who may have difficult accessing other refinancing options. Coupling zero closing costs for an increased interest rate may erode some of the value of refinancing to the borrower; however, some borrowers—particularly those with relatively high interest rates—may still realize savings through a zero-cost refinancing program. Further, while not explicitly listed within the research, if a refinancing program could be coupled with a program similar to down payment assistance for traditional borrowers, such may help households overcome liquidity constraints that prevent them from realizing the benefits of refinancing.

### **RELATED RESEARCH & COMMENTARY**

***Racial Differences in Mortgage Refinancing, Distress, and Housing Wealth Accumulation during COVID-19*** (Federal Reserve): Available at: <https://www.bostonfed.org/publications/current-policy-perspectives/2021/racial-differences-in-mortgage-refinancing-distress-and-housing-wealth-accumulation-during-covid-19.aspx>

***Almost 50% of Black and Hispanic Borrowers Could Save \$1,200 Annually by Refinancing*** (Freddie Mac): Available at [http://www.freddiemac.com/fmac-resources/research/pdf/20210512\\_black\\_hispanic\\_borrowers\\_save\\_refinancing.pdf](http://www.freddiemac.com/fmac-resources/research/pdf/20210512_black_hispanic_borrowers_save_refinancing.pdf)

***Black Homeowners Are Being Left out of the Mortgage Refinance Boom*** (*Money*): Available at: <https://money.com/mortgage-refinance-rate-race-gap/>

***Millions of Americans Refinanced Last Year—but Fewer Black and Latino Homeowners Did*** (*Wall Street Journal*): Available at: <https://www.wsj.com/articles/millions-of-americans-refinanced-last-year-but-fewer-black-and-latino-homeowners-did-11624440601>



***Mortgage Rates Are Low: Why Aren't Minority Homeowners Refinancing?*** (Knowledge @ Wharton): Available at: <https://knowledge.wharton.upenn.edu/article/mortgage-rates-are-low-why-arent-minority-homeowners-refinancing/>

***Black, Hispanic homeowners ended 2020 with less home equity than white borrowers*** (The Hill): Available at: <https://thehill.com/changing-america/560104-black-hispanic-homeowners-ended-2020-with-less-home-equity-than-white>