

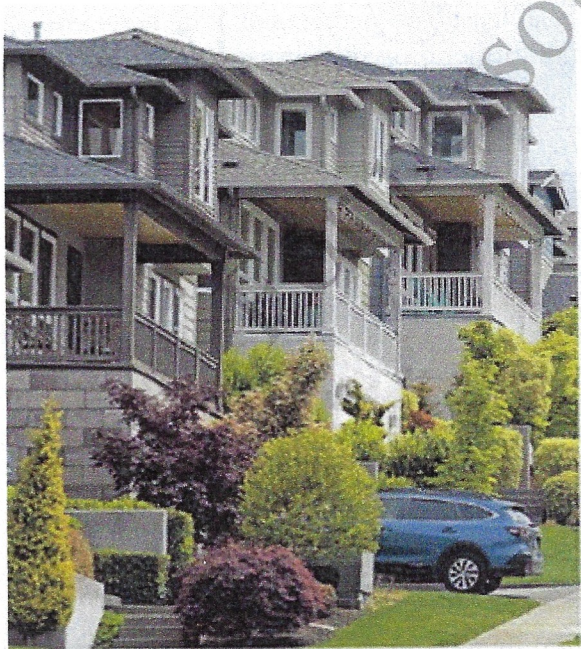
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Homeowners Leap on Mortgage Rate Dips

A small decrease in recent weeks triggered outsized response from borrowers

Blink and you will have missed the recent refinancing boom. The rush to lock in a cheaper mortgage was still a hopeful sign for lenders.

A minor move in mortgage rates triggered a strong reaction from borrowers. The cost of a 30-year home loan fell 0.3 percentage point to 6.26% over the three weeks through Sept. 17, which was the lowest rate in 11 months. Refinancing

activity jumped 80% over the period, data from the Mortgage Bankers Association show, but fizzled once mortgage rates rose again.

Borrowers are moving faster to lock in even small reductions in their housing costs. The financial incentive to refinance was actually higher back in September 2024, when rates fell to 6.08%, but fewer people took action then. They may have been waiting for costs to drop further and wound up frustrated when mortgage rates climbed instead. It has taken almost a year to get another opportunity.

What happens next matters not just to mortgage lenders but also the broader economy. Letting borrowers save on monthly payments or tap equity in their homes could become a key mechanism through which Federal Reserve interest rate cuts feed through to support consumer spending.

Most of the owners who refinanced in the latest wave were "marry the house, date the rate" buyers who purchased their homes within the past three years.

This group of borrowers has driven the lion's share of refinancing activity this year. In the second quarter, 90% of all rate-and-term refinancings were for loans originated in 2023 and 2024, according to ICE Mortgage Technology.

These borrowers have big mortgages as they haven't built much equity yet, so will feel the benefit of a lower rate. And they look stretched. People who refinanced in the second quarter saw their debt-to-income ratios drop to 34%—the lowest level since March 2022, according to Andy Walden, head of mortgage and housing market research at ICE. This will ease some pressure on household budgets.

At current mortgage rates, 3.1 million homeowners could reduce their rates by at least 0.75 percentage point and save \$399 on their monthly payment on average, based on ICE calculations. A small further drop in mortgage rates could motivate big numbers to refinance.

At 6%, 5.9 million mortgages outstanding would be in a position to shave 0.75 percentage point off their rates. This group of loans has an unpaid balance of around \$1.5 trillion. This could jump-start business for lenders who refinanced only around one million mortgages in 2024.

After an explosion of refinancings during the pandemic, when borrowing costs fell to historic lows, most mortgages outstanding in the U.S. have a sub-5% rate. These homeowners have zero incentive to refinance. Yet some of them are sacrificing their ultracheap loans to tap their swollen housing equity.

In the second quarter, borrowers doing cash-out refinancings took on a rate 1.45 percentage points higher than their in-place mortgage and raised their monthly payment by \$590 in order to withdraw \$94,000 of cash on average. For an owner who doesn't have a huge amount left to pay off on their home, this may be a cheaper option than other types of consumer debt like a personal loan. The interest payments on a cash-out refinancing are deductible if the money is used for home improvements, which is also the case for interest on a home-equity line of credit.

The bottom line is there is a growing backlog of borrowers who are waiting to refinance, and they are even more sensitive to rates than they were last year.

It may not take a huge drop in mortgage rates to unleash demand for lenders. That in turn could provide a useful cushion to consumer budgets, and the overall economy.

—Carol Ryan