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Should I switch to a fix rate?

The burning question I am asked a lot lately is: "Should I stay with a variable rate mortgage or should I fix?"

If rates are going to soar, then fixing would be a great strategy. But if they stay where they are or rise a little, it is a poor strategy. But, no one has a crystal ball, not even the smartest economists. So, let's look at what history tells us.

January 1990 saw interest rates rise to 18.75%. Most people had wished they locked into a fix rate loan just a couple of years earlier at around 14%. But then by April 1991, mortgagors were pleased they hadn't locked in because rates were now 13%. Eight months later they fell again to under 10%.

In 1992 people had the opportunity to lock in a 5 year fix rate at 10%, yet interest rates fell to just over 6% in mid 1993.

Are you getting the point here? People have little chance of picking interest rates in the next year or two.

But moving from variable to fixed will generally cost you from day one. So, if you fix today on a \$200,000 loan for five years you will pay close enough to 1.5% above variable rates. That will cost you \$3,000 a year.

If you were going to fix at 7.2% for five years, you must have worked out you can afford it. So, if you stay variable on our \$200,000 mortgage at 5.7%, you could

obviously put the \$3,000 a year into the mortgage, reducing your debt by around \$250 a month. When variable rates rise you will be paying the higher rate on a smaller loan.



Will this save me money over the long term?

So I see fix rates as a poor strategy, but good insurance.

Banks and capital markets are not stupid.

They agree rates are more likely than not to rise, so this is priced into three and five year loans.

So my answer to "Do I stay variable or fix" is not based on market movements which I cannot predict, but on historical logic. Stay variable and pay your mortgage off as fast as you can while rates are low.

They are at historical lows and history tells us historic lows are not sustainable. But the timing is uncertain.

“Time in the market is more important than timing the market”.

What to consider for your next property purchase

The current market is driving the perception that now is not a good time to buy, but in reality the truly smart investors are using recession-proof strategies to continue building their portfolios. Here are some common tips you need to put such a strategy into practice:

1. Choose property that’s attractive to tenants

It should be clean, have good sized bedrooms, off-street parking, and good positioning away from noise and main roads.

2. Choose property that will grow in value

If the property is close to a major CBD, beaches, schools, public transport and leisure facilities, it’s more likely to grow by more than the average in a good market and is more likely to hold its value in a down market.

If you buy around the median price then more people can afford to rent it, and more people can afford to buy it if you are put into a forced sale position.

3. Buy “blue chip”

Cheap properties are cheap because they are not in great demand and there’s plenty to choose from. It’s often better paying market value for a good property in a top suburb than getting a discount for something that no one else really wants. Time in the market is more important than timing the market.

4. Create instant equity

Do some quick renovations such as a paint job, re-carpeting, tidying the garden, painting the fence, installing new curtains or blinds, and replacing the kitchen-cupboard doors. For every dollar you spend on renovating, you should be aiming to get at least \$1 to \$2 back in the value of your property.

5. Refinance your property to create a buffer

When your property grows in value, refinance to create an emergency “buffer” zone. This will ensure you can continue to make mortgage repayments even if you lose your job.

Don’t find yourself in a forced sale position. You won’t get the best price and it may trigger capital gains taxes and other expenses.

6. Get a manager and re-sign your tenants

Hire a professional property manager to ensure you get reliable tenants and they pay a good market rent. Consider tying your existing tenant to a new 12 month agreement. This will help guarantee your rental income.

Traps in the fine print

One of our clients took out a home loan with ING Direct a few years ago, the contract she signed was very different to the contract that's been handed to her now. "Our original contract stated that I had a redraw facility attached to my home loan." "The other day I received a letter from my bank simply stating that this condition is changing. The bank was now able to suspend, reduce or cancel the redraw facility at any time and for any reason."

You can understand why this will make her nervous - with thousands sitting in her redraw facility she's worried that on any given day her bank can wipe away access to this cash. "Is this legal?" "Can they make such a significant change, considering that I have so much money available to me in the redraw facility."

Many home owners would be surprised to learn that they've probably already agreed to their lender being able to unilaterally vary the conditions of their loan, which many would consider unfair.

In today's economic climate it comes as no surprise they are targeting this particular feature.

Redraw allows home owners to stash any extra cash in their loan, thereby reducing the interest they pay, and at the same time giving them access to the extra funds whenever, and for whatever, they like. In this client's case those extra thousands was only a temporary deposit into her loan. "Now I know they can potentially reduce or cancel the redraw facility, having my mortgage with ING Direct is a risk I can't take", she says.

So what are her options? Most mortgage contracts do give lenders the right to cancel features such as redraw. Generally they would do this only if you are in arrears, but conditions surrounding redraws do differ between lenders. For instance, ANZ can refuse to provide further redraws if you are in default. NAB has taken upon itself to take one month's repayment out of all redraw facilities in a bid to protect its home owners from "inadvertently causing their account to become past due."

This client's home contract did stipulate that if she was in arrears or financial circumstances changed, the lender had the right to refuse to re-lend under the redraw facility. That's very different to the new clause that allows them to "suspend, reduce or cancel the redraw facility at any time".

For some home owners the answer may be to swap their redraw facility for a mortgage offset. An offset works in the same manner as a redraw, but it operates as a separate deposit account that has full transactional capability. Unfortunately for this client it isn't an option: "My lender doesn't offer mortgage offset, plus I've split my loan into a fixed and variable portion so I'd have to pay an exit fee if I want to refinance to another lender".

"For some home owners the answer may be to swap their redraw facility for a mortgage offset. "

FAQ

Q) What documentation will I need to supply for a home loan application?

A popular question for borrowers

1. 100 Points of identification (a passport **or** drivers licence & a debit/credit card will exceed the 100 point requirement). Make sure the photocopy of your identification is clear and that we sight your original identification during our appointment. NB: if your surname on any of the identification is different to your current surname you will need to provide a copy of your marriage certificate;
1. The **annual** rates notice on all properties that you own;
2. Last 3 months of credit card statements for each credit card account;
3. 2 consecutive pay slips (less than 4 weeks old);
4. Latest Payment Summary **or** tax return;
5. If you receive a Centrelink Allowance, then a copy of your most recent Centrelink statement is required;
6. For Purchases: Where your 'deposit' is held, the last 3 months **official** savings account statement **plus** an internet printout of savings transactions from the end date on your last statement up to today's date;
7. For Refinances: Where your 'salary' is paid into, the last 3 months **official** savings account statement **plus** an internet printout of savings transactions from the end date on your last statement up to today's date;
8. If you have a personal loan, we will require your last 6 months personal loan statement **plus** an internet printout of the transactions from the end date on your last statement up to today's date;
9. Your last 6 months home loan statement **plus** an internet printout of savings transactions from the end date on your last statement up to today's date.
10. If either of you are over the age of 50, then a copy of your recent superannuation statement is required; and
11. If either of you are self employed:
 - Last 2 years business tax returns and financial statements **and** last 2 years full personal tax returns
 - Your ABN
 - Accountant's full contact details



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We are a full member of the Mortgage & Finance Association of Australia (MFAA). We liaise with our panel of 25 residential lenders and 15 commercial lenders offering over 400 home loan products to find you the best finance structure and product to suit your specific needs. We specialise in housing loans, commercial finance, personal loans, lease finance, deposit bonds, general insurance and mortgage protection insurance. We organise immediate preapprovals, unconditional approvals, refinancing and answer any enquiries you may have. You deal with one professional from interview to settlement and beyond.