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Lenders crack down as borrowers clamour for fixed-rate mortgages

Near-record numbers of borrowers are fixing rates to cut costs and increase certainty about outgoings. But be aware of hidden costs.

by **Duncan Hughes**

Nervous lenders are enticing preferred home loan borrowers with big discounts as they renew efforts to weed out unsuitable loan applicants with tough new conditions excluding "less dependable" occupations and incomes.

Less dependable borrowers, say lenders, include those who rely on a high percentage of commissions or overtime.

The clampdown by lenders is not stopping record numbers of property buyers worried by recent rate rises out of cycle with official interest rates – and fearful of more to come – from applying for new fixed-rate deals to lock in repayments, say mortgage brokers. This is despite speculation this week that the next move in official rates will be down.

"Speculation that lenders will continue to lift their rates out of cycle with the Reserve Bank of Australia has meant a near-record number of borrowers are fixing part – or all – of their mortgage to avoid rising rates," says Jessica Darnbrough, a spokeswoman for Mortgage Choice, a national network of mortgage brokers.

Short-term special

Cheapest 1-year fixed rate mortgages (%)

Company	Product	Rates
Catalyst Money	Fixed	3.50
Illawarra Credit Union	Fixed	3.50
Newcastle Permanent	Residential Fixed	3.89
Newcastle Permanent	Premium Plus Package Residential	3.89
Queenslanders Credit Union	Fixed Rate	3.93

SOURCE: CANSTAR.COM.AU

Cheapest 1-year fixed rate mortgages

More than one in four mortgages house buyers are choosing a fixed rate, the highest in more than two years, it estimates.

Financial product research house Canstar estimates that more than one in six visitors to its mortgage products site are comparing fixed rates, a company record.

About 20 mortgage lenders have discreetly increased loan rates in the past two months. The lowest standard variable rate is 3.85 per cent, the highest is 6.11 per cent.

The 2.26 per cent spread between the highest and lowest standard variable rate is more than the official cash rate, which is 2 per cent, says Canstar.

Honeymoon specials

Top deals to attract rivals' customers

Lender	Product name	New rate
CBA	Guaranteed Intro Fixed 1 yr	4.39%
CBA	Wealth Package Guaranteed Intro Fixed 1 yr 150k+	4.39%
Community First CU	Honeymoon Fixed 1 yr	4.59%
Easy Street Fin Serv	Honeymoon Intro Fixed 1 yr	4.59%
First Option CU	Packaged Home Loan Investment Intro Rate 6 mths 60	4.10%
First Option CU	Packaged HL Intro Rate 6 mths 600k+	4.10%
Hume Bank	Honeymoon Intro Fixed (refinance) 1 yr	4.05%
Hume Bank	Honeymoon Intro Fixed 1 yr	4.05%
Hume Bank	Property Package Honeymoon Intro Fixed (refinance)	3.95%
Hume Bank	Property Package Honeymoon Intro Fixed 1 yr 150k+	3.95%
Northern Beaches CU	Honeymoon Fixed 1 yr	4.59%
Northern Inland CU	Fixed Honeymoon Owner Occupied 1 yr	4.09%

SOURCE: CANSTAR

Nervous lenders are enticing preferred borrowers with big discounts.

Lenders are growing more nervous due to the increasing costs of funding loans, rising regulatory expenses and pressure to ensure that borrowers can repay their mortgages in the event of an official rate rise.

For example, P&N Bank, one of the nation's largest mutual lenders, is making it harder for applicants with "less dependable" jobs to qualify for loans, indicating a new phase in policy intended to slow loan growth and stay within regulatory guidelines.

The lender is telling brokers that "certain income types" will have applicants' annual total of overtime, allowances and commissions "shaded" – or reduced – by 20 per net when assessing their eligibility for a loan

Police, nurses, teachers, firefighters and prison offers are defined as "dependable" and

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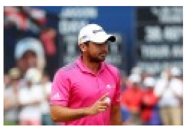

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will not have their overtime payments automatically reduced.

All other occupations where total income is supplemented by irregular payments – which could include bankers, sales people or farmers – will be reviewed.

The big banks have also been toughening lending criteria with measures ranging from lower loan-to-value ratios through to limits on the use of negative gearing.

But there are big savings for a qualifying loan applicant.

For example, a house buyer with a $1 million mortgage who switches from the average 4.77 standard variable rate to a 3.5 per cent one-year fixed loan would save about $740 a month in repayments. This equates to nearly $9000 over the term of the offer, says Canstar.

The accompanying tables show the top fixed-rate loans and a separate category called "honeymoon" rates, which are an inducement to win new fixed-rate customers from competitors.

"Honeymooners [those switching from other lenders] can certainly save money in the short term – just be aware of the increased costs down the track," says Justine Davies of Canstar. "They revert to significantly higher variable rates once the honeymoon is over."

A lender borrowing $1 million on a 30-year term would repay $5010 a month.

At the end of 12 months, the loan would revert to the standard variable rate of 4.9 per cent and monthly payments of $5315.

A smarter strategy would be, for example, to switch to CBA's standard one-year fixed rate of 4.54 per cent and monthly repayments of $5099, or a monthly saving of more than $200.

CBA has a special $1500 cashback offer on refinances of at least $250,000 that would comfortably cover set-up fees. These are indicative of current deals and may, of course, change over time.

Borrowers need to consider the term of the fixed rate, which can range from one to 10 years, and what it reverts to at the end of the term. These can vary considerably.

As a guideline, the average standard variable rate of more than 1100 home loans monitored by Canstar is 4.77 per cent. When your fixed loan ends, check the prevailing rates at the time.

"Regardless of the term, the loan rate reverts to the lender's standard variable rate at the end of the term," says Darnbrough. "That could be significantly higher than your current interest rate," she says.

"It pays to stay on the ball and revisit your finances before the end of the term."

Mario Borg, principal of Mario Borg Strategic Finance, a property consultant, says a fixed rate allows "set" repayments for a pre-arranged period, which is "an excellent strategy for those wanting certainty about cash flow commitments".

But there are also disadvantages a borrower needs to be aware of before committing.

A fixed term could also mean sacrificing some flexibility. For example you can't make additional loan repayments or switch products – or lenders – before the term expires.

Borrowers who pay more than the maximum repayment amount can be penalised for breaches of mortgage terms.

Also, most lenders do not allow a 100 per cent offset account against a fixed rate mortgage and prohibit redrawal of extra repayments until the fixed term has expired.

A compromise solution might be a split mortgage, which means it is divided between fixed and variable repayments.

That allows increased flexibility with a higher degree of certainty about repayments than a variable product.

Borrowers who try to break their fixed rate before the end of term will incur penalties to compensate the bank for potential losses.

Also remember that the longer the term of the loan, the greater the possibility it might fall behind comparable products because of rate changes.

"Ask the lender before taking the loan about charges for early repayment and build the cost into your overall assessment," says Darnbrough.

Property investors choosing a fixed rate should also check with their lender if there are any conditions to releasing equity for another property.