Fact or Fiction?

5 regular home loan misconceptions

1. A 100% offset home loan will save you money throughout the lifespan of the loan.

Fact: However the catch here is that the amount you 'maintain' in the offset account determines the savings per month. For example, if your home loan rate was 5.5% and you maintained $10,000 in your offset account for the entire month, the interest savings would be around $45 for that month, $50,000 would be $220 and $100,000 would be $450, is a general guide. If the offset money leaves the account as quickly as it goes in, the benefits to the account holder will be minimal as the interest savings are calculated daily against the balance of the offset account.

2. Having your properties financed with multiple banks will better protect your assets.

Fiction: Regardless of who your loans are established with, if you default on one loan a lender will take further funding, which can mean you sell off your assets – even if they are with another lender. For example, if you own two properties (house A and house B), and have each financed with a different lender (loan A and loan B). If you default on loan A the lender A sells house A. However if there is an outstanding amount owing, lender A can legally force the sale of house B with the loan B lender if necessary.

3. A fixed home loan offers the same benefits as a variable home loan.

Fiction: Although fixed home loan rates provide security ensuring that rates won't change for the period that you have chosen to fix, there are limitations if a customer wishes to pay off substantially more than the minimal monthly repayment within the fixed period. Most lenders offer a token amount that you can pay off as extra per year but it typically has little impact on substantial debt reduction. To manage this situation better you can usually take a portion of a home loan as fixed, to secure a specific rate at a specific time, whilst keeping an amount of the total loan 'variable', allowing for extra repayments and/or a 100% offset account against the variable portion at anytime with no restriction. This option can offer the best of both worlds if organised correctly. Currently in Australia you can fix a home loan from 1 to 10. Typically most borrowers fix between 2 – 5 years.

4. A 20% deposit is necessary to attain your first home loan.

Fiction: Most major banks in Australia offer Australian residents up to 97% lending against a residential property regardless if it's your first or 10th home loan. This is subject to meeting the banks criteria for both a borrower and the property being used as the security for the loan. The catch to be considered when borrowing above 80% of a property's value is the one off, upfront lenders mortgage insurance fee (LMI) which increases pending the percentage of the homes value used in conjunction with the dollar amount borrowed. To remove mortgage insurance fees entirely when borrowing up to 100% of a property's value, many first or even third time home owners chose to a 'guarantor' option which splits the required home loan between the (a) new home purchase and (b) a second property provided by the 'guarantor' via a 80 /20 percent split. This is again, subject to the meeting of specific lenders criteria, available income of the borrower and the available equity held within the guarantor property.

5. Numerous monthly repayments will pay off you loan faster.

Fact: The interest on a mortgage is typically calculated daily and charged monthly. So making more regular repayments per month will reduce the amount of interest paid as it reduces the time for interest to acquire during the repayment period. For instance, making fortnightly repayments for a year, will add up to the equivalent of 13 monthly repayments due to there being 4.3 weeks per month. Most banks offer weekly repayment options which has an even greater impact on debt reduction over the life of a loan. Remember this benefit is only relevant when you are making principal and interest repayments.

Summarising:

a) Maintain a constant or increasing balance in your offset account to maximise the benefits on an offer.
b) Splitting your borrowings between different lenders does not protect you nor will it increase the extra rate discounts available from lenders.
c) Weekly mortgage repayments save you interest and time more than fortnightly or monthly repayments especially when making principal and interest repayments.
d) A fixed home loan generally restricts how much extra you can pay off per month whilst within the fixed period.
e) Many major lenders today offer first, second or even tenth property buyers the opportunity to totally remove mortgage insurance costs whilst borrowing 100% of the property value via a 'guarantor' structure.

Want to know more or have a tricky finance question that you need advice on?
We are a call / e-mail away with an answer.

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