Knowledge bank- Trusted Finance Solutions

Latest on investor loans and how you may be impacted.

Daryn Heffernan

A few months back, we wrote about the changing landscape for investors seeking finance.

To summarise, the Australian Prudential Regulation Authority (APRA), feel that the property market in parts of Australia is too hot and is trying to put the brakes on. APRA is keen to restrict the growth in investor loans to no more than 10% p.a. They know that the more freely available credit is, the greater the chance of bubbles forming. As a result, they are making the banks they govern increase their capital requirements and it estimated that the big four banks and Macquarie for example, will need hold about $1 extra in funds for each $100 of housing loans.

In response, the banks initially made the following changes:
– Reduced LVR's on investor loans, in some cases to a maximum of 80% of purchase price
– Reduced the interest rate discounts on investor loans
– Removed the refinance rebates / cash rebate on investor loans
– Increased their benchmarks on investor loans
– Policy changes to investor loans

However, over the last few weeks, the banks have gone one step further and are now increasing the interest rates on investor loans. As a result, many of the banks now have different interest rates for investors and owner occupiers. The standard variable rate for an investor loan is moving approximately 25 to 30 basis points higher than owner occupied loans in the coming weeks whilst the banks are again pricing (offering larger discounts) for owner occupied loans only. What this means is that the approximate difference in interest rates (comparing an owner occupied loan to an investor loan), could be between 25 to 50 basis points shortly, depending on the bank.

The question then must be asked, will the banks stop there or will the gap widen further? Our sources in the banks are stating that the gap between investor and owner occupied interest rates may widen over the coming year to 100 basis points.

Also take note that in many cases, depending on the financial institution, the interest rates on investor loans are increasing for both new and existing loans.

Trusted Finance Solutions View –

The issue we have with this is that if the banks want to slow the future investor market, why are they increasing the interest rates for investor loans that have settled years ago? The answer to this can only be that they want to increase all investor interest rates to compensate for the APRA requirements of holding more capital so that their margins are not impacted.

In addition, the general consensus is that there is not enough supply of property, hence making the prices too high for first home buyers to enter the market. We are unsure how keeping investors from purchasing land and building investment properties, will increase the supply of properties. If anything, it will make the situation potentially worse.

Furthermore, those that have bought an investment property off the plan and were seeking 95% may now have difficulty in settling, impacting their deposits. It also makes it more difficult for developers to sell their properties, once again, slowing properties coming on to the market.

There is no doubt that these changes will have an impact and slow both credit and property growth and time will tell if APRA has been too aggressive, especially given only two states in Australia are seeing large price growth.

Some of the changes that have taken place over the last few weeks:

– NAB has increased their standard variable rate on all existing and new interest only variable loans (both owner occupied and investment) by 29 basis points commencing 10/08
– CBA has announced it will increase their standard variable rate by 27 basis points for new and existing customers, commencing 10/08.
– ANZ has announced it will increase their standard variable rate by 27 basis points for new and existing customers, commencing 10/08.
– WBC (Westpac) has announced it will increase their standard variable rate by 27 basis points for new and existing customers, commencing 10/08 for new loans and 25/09 for existing customers.
– BOM (Bank of Melbourne) has announced it will increase their standard variable rate by 25 basis points for new and existing customers, commencing 21/08
– AMP has announced it has pulled out of all investment lending and will increase their standard variable rate by 47 basis points for new and existing customers, commencing 07/09.
– BOQ (Bank of Queensland) has announced it will increase their standard variable rate by 29 basis points for new and existing customers, commencing 10/08
– Suncorp has announced it will increase their standard variable rate by 27 basis points for new and existing customers, commencing 31/08
– First Mac, is not governed by APRA, has increased rates on investor loans by 25 basis points.
– Macquarie has announced it will increase their standard variable rate by 27 basis points for new and existing customers, commencing 31/07 for new loans and 10/08 for existing customers.
– ING has announced it will significantly increase the rates for new investor loans but will not increase existing investor loans.
– Most of the above financial institutions have also increased fixed rates for investment loans.
– At this stage, Citibank does not seem to be loading investor interest rates. This is subject to change.

Good summary of some of the banks:
http://www.news.com.au/finance/business/banks-act-on-investor-home-loan-growth/story-e6frfkur-1227464715727

What should you do?

Don't panic:

Firstly, for those with investment loans, there is no need to panic but if you do have a large portfolio of investment loans, it is certainly worth reviewing your position. Keep in mind, the interest rates on offer are still the lowest most of us have seen so we need to be realistic that at some point, rates were always going to rise. The difference is that we all assumed that the RBA would start increasing rates in the distant future given they have an easing bias currently. However, in this case it has been the banks increasing rates outside of RBA announcements.

The other reason not to panic is that not all financial institutions have made a decision on what they are doing with investor loans and hence to refinance to try and pick up a lower rate may look good today, but may cost you when the bank you move to decides to increase their investor loans as well. Therefore, a refinance could be a good option to pick up a lower rate moving forward but I would urge caution until the dust settles.

Blended rate:

Keep in mind that if you have both owner occupied and investment rates, your overall interest rate will be somewhere in the middle, creating an average or lower "blended rate".

Fixed rates:

You always have the ability to lock in an interest rate at any time to secure your future cash flows and for an investment loan, this may be a good strategy, especially if the gap between investor interest rates continue to increase over the next year. Keep in mind the pros and cons of fixed rates. The negative with fixed rates is that:
– They are less flexible and you normally cannot make large credits to the loan during the fixed rate period.
– You generally cannot have offset accounts linked although we do have some banking options that allow this.
– Can cost you if you pay the loan out before the expiration of the fixed rate term. Ie break costs.
– The banks normally win most of the time when it comes to a customer locking in a fixed rate.

SUMMARY –
– Everyone's situation differs so it is important to touch base with us if you would like Trusted Finance Solutions to provide advice for your specific situation.
– Banks will determine the interest rate based on purpose, rather than loan size in the current climate.
– Owner occupied, principal and interest loans are not impacted. The banks are aggressive in this space and are offering large discounts to win this business. We are seeing banks reduce owner occupied variable and fixed rates and refinance cash rebates have now increased to $2,000.
– However, owner occupied, interest only loans may impacted, depending on the bank, such as NAB outlined above.
– Non Banks or some of the smaller players are not governed by APRA. Hence, this is a great opportunity for them to keep investor rates low and pick up market share. However,

I can confirm that some non-banks such as First Mac, have announced investor loans increases in recent days.
– We are moving into new territory. It is becoming increasingly more difficult to find solutions for investors with large portfolios. With banks policies for investors tightening and investor rates rising, moving forward, obtaining finance will be more about getting the deal done, rather than the lowest rate on the market. Chasing the lowest rate may mean you have to take a principal and interest repayment for example which may not be desirable for an investor wanting to manage cash flow.

Please contact your Trusted Finance Solutions credit adviser should you need any advice on the above.

Credit reporting: Will a bank lend to you?

Daryn Heffernan

Firstly, your credit report is what all banks use as one of their tools to determine if they will lend to you.

Up until 2014, Australia had a "negative credit reporting" system which meant the credit report mainly looked at "negative" information about your credit history such as possible defaults and judgements.

The laws regarding credit reporting changed in 2014 to a new system, similar to many countries overseas, known as "comprehensive credit reporting". These changes give credit reporting bodies more detailed information about you, which then allows the banks to make a more informed decision.

The new credit reporting system still outlines defaults and judgements but also covers whether credit you have applied for has been approved or declined, the amount of the credit applied for and even if you are making those repayments on time. Also listed will be whether the approved loans have interest only or principal and interest repayments for example.

In summary, the new credit reporting will be a lot more comprehensive and this information is being shared between financial institutions.

You have the right to obtain a free copy of your credit report at any time and you can receive a free copy if you can wait approximately 10 days. You may have to pay if you need the report sooner.

You can get a copy of your credit report from the following credit reporting agencies. Please note, in some cases, you may have a credit report with more than one agency.
Credit reporting agencies

Veda.com.au
PO Box 966, North Sydney NSW 2059
membership.query@veda.com.au
Phone 1300 762 207

CheckYourCredit.com.au (Dun and Bradstreet)

PO Box 7405, St Kilda Rd, Melbourne, VIC 3004
pac.austral@dnb.com.au
Phone 1300 734 806

Experian Credit Report
GPO Box 1969, North Sydney, NSW 2060
creditreport@au.experian.com
Phone 1300 783 684

Tasmanian Collection Service
GPO Box 814, Hobart TAS 7000
enquiries@tascol.com.au
Phone 03 6213 5555

What is Lenders Mortgage Insurance (LMI) and when does it apply?

Daryn Heffernan

The key level for the majority of banks is 80% LVR (Loan to Value Ratio). If you borrow 80% of the purchase price, it means you have to come up with 20% of your own funds plus costs (such as stamp duty) to complete the purchase.

At 80%, the bank feels that you are contributing enough “hurt money’ to give them comfort that if something were to go wrong and the loan was not able to be repaid, they should be able to recover the initial loan amount given the “equity” already in the property.

However, if a loan at 81% was requested, (ie $405,000 loan on purchase price of $500,000), as the level is greater than 80% LVR, the bank feels they are taking on slightly more risk and as a result, take out an insurance policy with an insurer to cover the bank in the event that you default on the loan. The bank then passes on the cost of the LMI to the borrower in the form of an LMI premium which is either paid by the borrower upfront or added to the loan amount. This is a one off fee/premium charged at settlement of the finance.

The higher the LVR (all the way up to 95%), the greater the LMI premium.