The 3 minute Mortgage Hero™ Wisdom series

Fixed Rate Pros and Cons

Brought to you by the 3 minute mortgage hero™

What is a Fixed Rate loan?

Fixed rate loans give you the ability to set your interest rate (and your repayments) for a fixed period of time. Most lenders have fixed rate loans with terms of 1,2,3,4 and 5 years.

During the time you have your loan fixed for, your repayments will not change even if your lender rates increases or decreases their interest rates.

What are the advantages of fixing my loan?

A fixed rate can offer security and knowledge of your ongoing repayment especially in times of economic turbulence or uncertainty.

Depending on when the fixed rate is set up, it can offer you the opportunity to get a significant low rate for a long period.

A fixed rate may potentially suit one type of client over another, ie a long-term Investor may want certainty of repayments and not need to pay any extra into the loan or First Home Buyers who may be on a tight budget and so are looking for the longest possible lowest rate and may not have any extra funds to contribute.

What are the disadvantages of fixing my loan?

A fixed rate home loan works in a very different way to a variable rate home loan.

If your lender decreases their interest rates during your contracted fixed rate period, your rate and repayments will not change and you may be fixed at a higher rate than you possibly could have with a more flexible variable rate.

With a fixed rate, you lose a lot of the flexibility you have with a variable loan and may face high break fees if you make changes to your fixed loan or exit the fixed loan during the contracted fixed rate period,

These break cost fees can be a significant amount (fees can be several thousands of dollars) depending on when you break the loan. There are several factors which determine what the break cost fee may be, and your lender would need to advise you of the costs involved.

If you plan to sell your property or refinance within the fixed term, then you may incur large break costs (as above).

If you have the need to make large extra repayments or think you may be coming into some extra funds that you want to pay into the loan (ie an inheritance or bonus payment) then fixing may not be suitable.

Most lenders will cap the extra repayments you can make on the loan (typically this is up to $10,000 pa, but varies by lender) so if your aim is to pay off the loan quicker using large extra repayments, then a fixed rate may not be suitable. Lender fees may be applicable if you overpay the loan.

Obviously unforeseen circumstances do occur, but the key is to understand if you will have any reasonably foreseeable events which may make it unsuitable to fix your loan.

What is a Rate Lock Fee?

A Rate Lock Fee is an optional non refundable fee lenders will charge you to guarantee you receive the fixed rate you have applied for. This is usually paid at the time of the loan application and the cost will vary between lenders.

It is important to understand that a fixed rate may CHANGE between the time of choosing a fixed rate loan and the actual loan settlement. Some lenders will apply the fixed rate on the date you apply, some on unconditional approval and others will apply the fixed rate on the settlement date.

The Rate Lock Fee basically guarantees you receive either the rate you applied for or a lower rate (at the same loan term) if there have been any downward rate changes prior to settlement; if the rate increases then you will get the lower rate you applied for.

It is important to understand how your lender manages the process and at what time they apply the interest rate, this will allow you to make the choice to pay the Rate Lock Fee or not.

All information provided as a guide only, if you need specific help with your lending requirements please contact me below.

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