Which Home Loan?

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Owning a home is a big part of our culture in Australia

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Introduction

Owning a home is a big part of our culture in Australia – the great Aussie dream. We are a country full of people from all walks of life and from all corners of the world. And the freedom of being able to take a share in this great land and make part of it our own is nothing to take for granted.

And the facts are that unless you have saved relentlessly over many years, have won lotto or have the benefit of a wealthy family – you will need to borrow money to be able to afford your home, or investment.

In writing this book – we wanted to convey is that you have a choice. No longer should you feel obligated to go back to your bank who you have saved with since you were at school, or perhaps where mum and dad bank or where your mate at the BBQ suggested.

There are plenty of various lenders who are keen to win your business. The way you set-up your loan in the beginning can make a huge difference to the amount of interest you pay over the term of the loan. In our opinion: the more interest you pay – the less you will have in retirement (as those funds can be directed into other strategies to build wealth once your home loan is paid off) – and the faster you pay your home loan off the sooner you can start to save.

The intent of this book is not to convince you that Mortgage Brokers are the best in the world. Nor is it to convince you that going direct to the banks is the worst decision either. We want to give you information and then let you make a decision. We believe that most people are smart and when given the facts they will make an informed decision.

Any bias stems simply from the fact that often there is a better product, but often you don't know what you don't know.

We will first explain what a Mortgage Broker is and how they work. Next, we will explain how a bank works, and the obvious benefits of options and choice that come with using a broker.

In the next chapters, we will give you a cursory education about good versus bad debt, the different types of home loans available, and how and where you can get one! We will also give you information that you should ask before you decide which home loan is right for you and questions to ask before deciding on a loan provider. Finally, we will tell you about some additional services offered by Mortgage Brokers. We hope you learn and enjoy the read, and we look forward to working with you to secure your dream of owning your own home.

Kind regards

The Team at
Connective Member

1 What is a Mortgage Broker?



Mortgage brokers are professionals in the home loan industry. They work with you to determine your borrowing needs and how much you can borrow. Brokers help ensure you don't take out a loan that is too big for you.

Professional Mortgage Brokers only focus on loans. This means a broker is an expert in loans and when you engage a mortgage broker, you are engaging a loan specialist. If you have a toothache, you go to the dentist not a florist. If your car is broken you take it to a mechanic not a librarian. You go to someone trained to help you with your specific need. It's the same when you need a loan. The decision that makes the most sense is to go to someone trained in your specific need; a mortgage broker.

Since brokers are trained to handle loans and not so many other things, they have access to a wide variety of loans. At your local bank, the banker can only offer you loans that the bank finances and originates. A mortgage broker has access to loans from dozens of different banks and lending institutions. This means your broker can find a loan that is just right for you.



Let's imagine two fictional characters: Joe the banker and Richard the Mortgage Broker. Joe is able to offer you loans that his bank backs. Joe cannot offer you any other loans. Richard can offer you loans from dozens of different lending institutions, including Joe's bank. Richard simply has access to many more loans because he is a specialist.

Mortgage brokers also assist in spreading the wealth throughout the community. Most brokers are involved locally be it with their family who attend your local school, sponsoring sporting teams or community groups. They also employ staff who work and play in your local community. They own property and spend business income and personal income just like you locally. So personally we feel that this is a good thing – to have a small part of the income in our local community.

A mortgage broker has access to loans from dozens of different banks and lending institutions.

Mortgage Brokers & New Legislation

In the past, prior to legislation in our industry, going through a mortgage broker may have seemed ‘hit or miss’. This prompted many people to use a bank because it was seen as safer. New legislation has cleaned up our industry and rid us of unethical businesses.

This new legislation is called the National Consumer Credit Protection Act or NCCP. It’s designed to protect consumers and ensure ethical and professional standards in the finance industry, through the National Credit Code (NCC). All lenders and mortgage brokers are required to hold a credit licence or be registered as an authorised credit representative under a license holder.

The new national regulation for the credit industry, including mortgage brokers commenced on 1 July 2010. Changes include that credit for residential property, including residential investment property, is regulated nationally by the Australian Securities and Investments Commission (ASIC). Note that some state laws and regulations continue to exist, such as maximum interest rate caps in ACT, Qld, NSW and Victoria.

Finance broking contracts (FBCs), have been mandatory in NSW and Victoria until 31st December 2010. However, from 1 January 2011, a new phase of the NCCP is in effect that requires that Credit Guides and Credit Quotes be provided to potential borrowers. These documents are designed to give borrowers pertinent information about their rights and obligations under the NCCP.

Another very important aspect of the NCCP is the concept of “responsible lending”, because it requires all persons involved in the provision of credit for ‘personal, domestic or household use or consumption’ to make sure that the borrower is able to make repayments on a loan (or lease) without substantial hardship. In other words, loan products must be ‘not unsuitable’ based on the objectives and needs expressed by a borrower.

This legislation has made it safe and secure to use a mortgage broker. However, if you want to find the BEST brokers, you should seek one who is a member of the MFAA (Mortgage and Finance Association of Australia) or the FBAA (Finance Brokers Association of Australia). To become a member of either of these organisations an individual must have at least two years of relevant industry experience or a minimum standard of education. Members also must undergo continuing education and can apply for higher accreditations. However, the most important factor in hiring an MFAA or FBAA member is the their commitment to ethical practices. All members must adhere to an industry Code of Practice that demands high professional standards and adherence to both the letter and spirit of the law. These disciplinary procedures help rid the industry of predators and make it safer for borrowers.

Together, the NCCP Act and our industry bodies have changed the mortgage brokerage industry. A fully accredited and professional mortgage broker is now just as safe as going to your local bank.

Brokers work with clients to determine their borrowing needs and ability, select a loan suited to their circumstances and manage the process through to settlement.

Some benefits of using a broker:

- They do all the legwork for you
- Access to a wider range of loans
- Experts in a wide range of loans
- More flexible
- Greater expertise as they focus on loans only.

A fully accredited and professional mortgage broker is just as “safe” as going to your local bank.

What about fees?

Some mortgage brokers charge a fee and some don't. Perhaps you are asking yourself why go to a broker when you might be able to get the same loan at a bank? The reason for many people is because mortgage brokers are normally easy to get in contact with, are professional in what they do and have their finger on the pulse when it comes to getting accurate product information. They can provide you with options – not just one product that the bank wants you to sell for their own profit interests – and give you explanations about what the options mean for you in your particular situation. This is what Mortgage Brokers focus on and do every day.

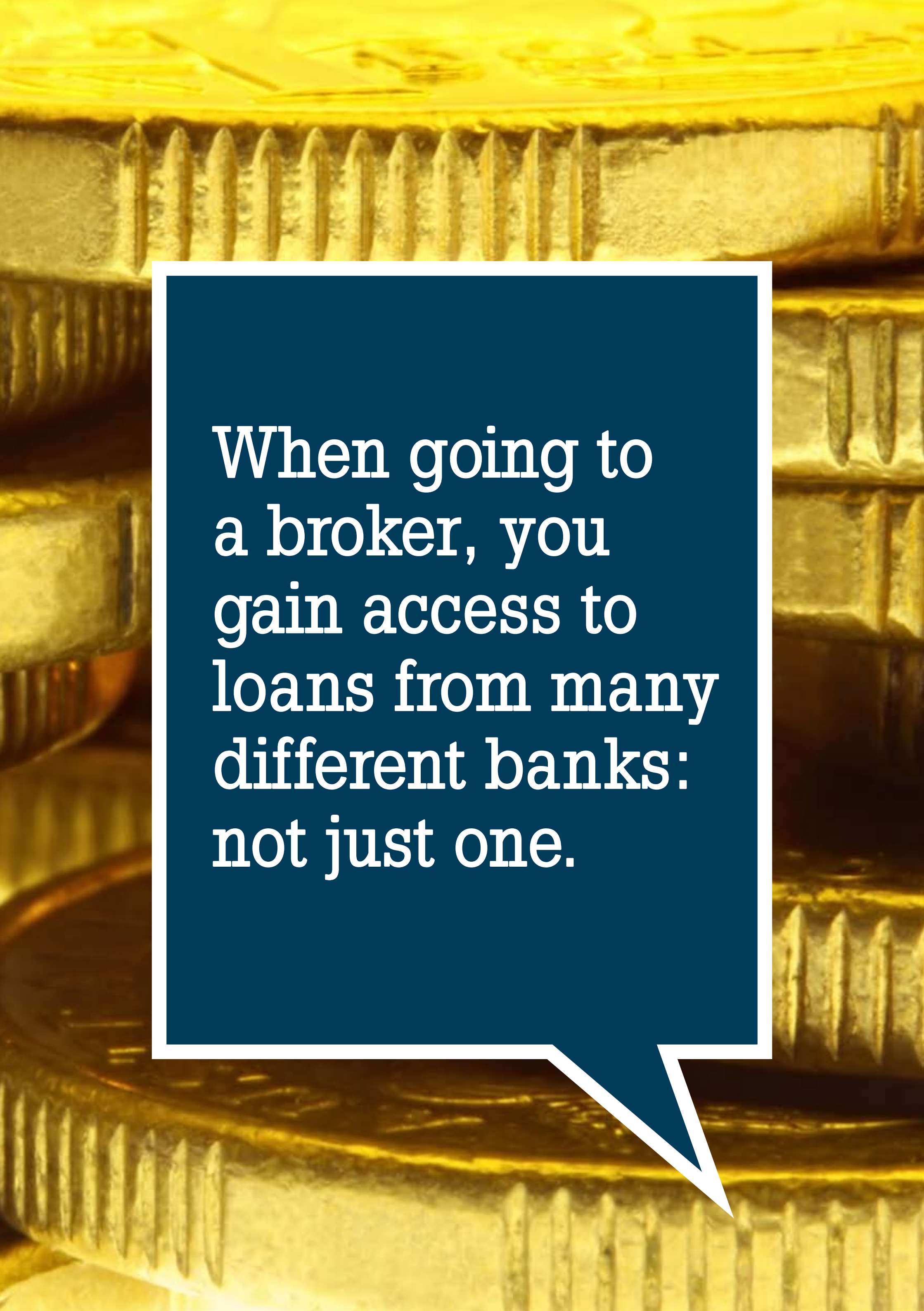
Commission from the bank
When you take out a loan via a Mortgage Broker – it does not cost you more. That is an absolute myth. Brokers get paid commission by the bank for bringing new business to them, and this does not impact your rate or level of service.

Nearly 50% of all new business to the major banks is now coming by way of Mortgage Brokers, and in our opinion it is on the rise. It will grow as more and more Australians see the benefits. The banks enjoy having business coming in via Brokers, as it is very profitable for them. You see they only pay a broker (typically 0.50%-0.65% of the loan amount) when they get the business referred to them. So they are not carrying the fixed and often expensive costs of mobile bankers or the branch manager's salary, or the rent, or car and laptop and mobile, etc. Rather they just pay a referral fee when they get the new business in the door.

Fee for Service
Some brokers charge a fee for their service. They must disclose this fee upfront to you so you know what you will be up for if you engage their services.

When going to a broker, although you may pay a fee, you gain access to loans from many different banks: not just one. For some people this presentation of greater choice is well worth the small fee they pay.

Finally, the level of personalised customer service at a broker is just much higher than at a bank. A broker is part of your local business community and as such is dealing with many other like minded businesses that they could refer you to. If you are paying a fee – then that broker will understand that it entitles you to be treated better and get better services. However, many brokers who don't charge a fee are dedicated and focus on giving excellent service and product recommendations. At the end of it all – if a broker cannot demonstrate to a prospective new client good enough reasons to do business with him, then he will not be paid.


When going to a broker, you gain access to loans from many different banks: not just one.

2 Getting your loan direct from a bank

Whilst mortgage brokers offer you better service and a wider range of options for your home loan, you may also wish to go direct to a branch. As we mentioned in the earlier section, there is a certain misconception that going direct to a bank means that your loan is safer. However, this is not the case. Due to NCCP using a mortgage broker is just as safe as going to a bank, and it also means that you get a better range of products.

When we talk about a ‘loan product’ we are referring to the thousands of options that are currently available for you for your loan. Each bank (or lender) has loads of different loan options – low doc, package loans, re-draw facilities, plant and equipment loans, fixed, interest only, interested in advance, variable, introductory variable... the issue you face as a consumer is ‘Which loan is right for me?’ And that is where a mortgage broker comes in.

The purpose of this information booklet is not to turn you off going to direct to a bank, it's to give you the information you need to make the right decision for your financial future. If you go direct to the bank, you will only be offered the loan options available through that one lender – not the full spectrum of loans that are out there. And you know what? You're going to have to visit a lot of branches and have a lot of conversations before you can gather all the information you need to make a decision.

As your mortgage broker, we do all the leg work for you. We are across over 50 lenders and all of their loan products and our sole purpose is to find the right loan for your needs. And when those needs change… be there to help you make the next financial decision when it comes time to renovate, have a baby, or go on holidays!

> If you go direct to the bank, you will only be offered the loan options available through that one lender.

3 Traditional Mortgages



A Mortgage is a method for borrowing money to pay for a specific physical asset, such as a house for consumers or plant and equipment for a firm.

In a mortgage, the lender loans a specific amount of money to the borrower at some interest rate. The borrower, that's you, makes a fixed payment each year (monthly for home mortgages).

In a mortgage, the loan is fully repaid (both principal and interest) when the last payment (monthly or annual) is made. That's your goal!

The mortgage payment is calculated to include both the principal payments which pay back the original amount of the loan, and the interest payments which are calculated by multiplying the interest rate times the unpaid balance of the loan.

Over your working life you will potentially earn millions of dollars. The problem is, it costs a fortune to live even a modest lifestyle and, as the following example shows, paying off your home mortgage is your biggest problem. The key is to learn how to get your money working for you, instead of against you.



Example:
On a $300,000 mortgage at 7.25% over 30 years, a total of $736,749 is actually repaid. This means $436,749 is paid in interest, or put another way, almost one and half times more is paid in interest over the 30 year term, than the amount borrowed. After 18 years of making monthly mortgage repayments of $2,046 you would still owe approximately $300,000. Unless you pay your home off quickly, it is unlikely that you will ever achieve your financial goals! You work to earn an income, you pay tax, and your ‘after tax dollars’ are then used to pay off your personal debts, which includes your mortgage. In this example, you would need to earn approximately 1.4 million dollars before tax, over the 30 year term, to repay a loan on your home of just $300,000! A mortgage professional can give you a health check on how to best set up a loan so you pay less to the bank over time.

Assumptions: Interest rate of 7.25% remains constant over the term of the loan; repayments of $2,046 remain constant over the term of the loan; the same loan is kept for the full 30 year term; borrowers are in the highest tax bracket (46.5%).

4 Good Debt Vs Bad Debt



Living life creates debt. Owning your own home, cars, dining out, and generally enjoying life, all costs money – money that is typically borrowed from a financial institution. While debt is an essential part of everyday life, it can also wear out its welcome, and wear down your desire to dream for a better tomorrow. One of the reasons why so many Australians are restricted in their ability to achieve their financial goals is because they are simply 'drowning' in debt.

When you are deep in debt, you restrict your ability to build wealth before you've even had the chance to start. That's why you need an effective debt elimination strategy, a customised plan of action, and a clear understanding of the difference between 'good' and 'bad' debt.

The difference between these two types of debt can be distinguished as follows:

Bad Debt

- Is used to make lifestyle acquisitions
- Does not generate an income stream
- Interest cannot be claimed as a tax deduction
- The interest and the debt needs to be repaid from personal 'after-tax' income
- Must be eliminated as quickly as possible



Smart Debt

- Is used to acquire investments
- Generates an income and appreciates in value
- Interest is tax deductable
- Income generated from investments is used to pay off the debt

Since the debt is largely self-funding, there isn't the same urgency to pay it off. A loan used to secure a residential investment property is an example of smart debt. Financial independence is within your reach. Financial independence is the result of building wealth and this requires discipline, the discipline to consider every dollar you spend and every dollar you save, because wealth (unless it's handed to you) takes time and commitment to accumulate.

A qualified mortgage broker can assist you in setting up strategies to maximise your good debt whilst repaying your bad debt faster. And overall getting to zero debt faster!

5 It's More than the Interest Rate

Interest rates are important and they are an important factor to consider when deciding which loan is right for you. A higher interest rate can mean thousands of dollars over the life of your loan. So, getting a nice low rate is certainly something you need to make certain you do.

However, purchasing a home is the biggest financial decision most of us will ever make. Make sure you consider all the factors before you jump in.

So, what else is there to look at? Well, there is the type of home loan you want. A Basic Home Loan doesn't have many frills and is often a variable interest rate. There aren't any impressive fees and there isn't any option to pay off early or pay more than your required amount. These are great for people who don't foresee any dramatic life changes coming soon.

Let's add two more fictional characters to our repertoire: Cindy and Lee, the home buyers. In this example, Cindy and Lee are buying their first home and expect to stay there for at least a few years. They don't expect to get married or have kids in the near future. Their jobs are stable and they think they will be employed for the foreseeable future. A **Basic Home Loan** is right for Cindy and Lee. They are unlikely to have access to extra funds to pay down the principal faster or be able to effectively use an offset account to the degree that it will make a significant dent in the short term – so rather than pay extra fees and perhaps a higher interest rate – a Basic loan may be more appropriate.

The next type of loan is a **Honeymoon loan** – or Introductory rate loans. These offer a very low fixed or variable interest rates for about 6 or 12 months, after which time, the standard rate applies. These are good for folks who want to do renovations and pay as little as possible on their mortgage during that time, or for people who want to make a large dent in their repayments while the interest rate is still low.

Cindy and Lee just bought a “fixer upper.” It was all they could afford after paying for their lavish wedding. However, they have some income leftover every month to pay to do the house up.

The Honeymoon loan would be good for them to fix up the house a bit, before the interest rate rises. However once the rate comes off the Honeymoon period – usually the interest rate is quite a bit higher and it is a shock to the budget and system when you are used to paying a smaller monthly payment.

Another popular type or feature is the **Redraw Loan**. This clever loan allows you to save for the future while paying down your principle. This loan allows you to put extra funds into the loan, thus paying off the principal. If you need the money in the future, you have the option to withdraw it.

Cindy and Lee are now looking to have children and would like to save for the period when Cindy is not working. They get a Loan with a redraw feature. Every month, some extra money is placed into the loan. The principal is paid down with the extra money. However, if a “rainy day” ever hits, or she wants to take 6-12 months off work – they can withdraw that money. It’s a great safety net. If they never need the money then they have access to the extra principal that they have paid off the loan.

The **Equity Line of Credit** is also quite in fashion. This is similar to a big overdraft and at home loan rates. These loans are popular with people looking to gain access for investment or renovations, or perhaps people on commission only type roles – because they are interest only – and all your income sits in the one account making it easier to pay down. They often require very good budgeting and control – as the amount of principal you pay off your loan is solely determined by you.

Cindy and Lee already own a home but it’s old and in need of renovation. They get an Equity Line of Credit. They use their home as collateral and get $50,000 to renovate the bathroom and kitchen. It was easier for them to gain access and only pay interest on what they used – rather than getting the whole $50,000 in a lump sum and paying interest on the full amount. Also, they are adding value back into their home by doing the necessary renovations. However, the money borrowed does not have to be used within the home. You can use the money for anything (legal) you like.

There are many more types of home loans, but these are the most common for the typical home buyer.



You can even split a loan into part fixed and part variable; well, your mortgage broker can. As you can see, from just these few types of loans, interest rate matters, but so do other factors. With the bewildering varieties of loans, and loan terms and conditions available it can be easy to lose your footing, especially if you are a first-time home buyer. A mortgage broker can sit down with you and guide you through the process, while ensuring you get the loan you need.

A broker has access to so many more loans; in fact, some loans are only available to brokers. With that in mind, your broker will show you a few loans that fit your needs, and you can choose the one you like the most. These sorts of options and this level individual customer service is only found through the best brokers; MFAA brokers. Remember, the MFAA requires members to have a high level of education and ethical standing. The MFAA also has guidelines in place for removing members who do not continue to meet the standards. So, when you hire an MFAA mortgage broker, you can rest assured that the member is in continued good standing.

Richard is an MFAA member so when you go to see him you will receive a consultation that will cover every area of your home buying solution. You won't need to complete lots of paperwork because Richard and his team will take care of that for you. Additionally, when you call Richard, he answers the phone or calls you back as soon as possible. That is the commitment MFAA members make to service and choice.

6 Questions to Ask First

Before you meet with your mortgage broker or banker for the first time, there are some questions you should be prepared to ask. These will help you make certain you get the right loan for you; not just for today but also for tomorrow. After all, this loan will, most likely, last for years!

Questions to Ask about a Suitable Loan for You

- What types of loans are available?
- The mortgage broker and bank will offer different products.
- Will I have to take out Lenders Mortgage Insurance?

This insures the Lender, not the borrower, and gives the lending institution the ability to lend over 80% of property value. LMI is a once only fee that is paid at the time of loan settlement. It can often be added to the loan.

- What percentage of the property value can be borrowed?

Question to Ask about the Loan Product

- What is the interest rate?
- Does it come with an Offset Account?
- Is it variable or fixed?
- Can it be split?

Remember, some loans can be split into part fixed and part variable.

- What are my weekly/monthly repayments?
- How much is the loan establishment fee?
- What does the loan establishment fee cover?

  For instance, many cover valuation and lender's legal fees.
- Are there any ongoing fees?

  These are often service or maintenance fees.
- Will the lender give pre-approval with no upfront fees?
- What is the level of service after settlement offered by the lender?

  This question is best answered by someone with quite a few years of experience in the loan industry.
- Do they offer internet banking, EFTPOS, branches, and ATM? Are there any additional fees for these services, and if so, what are the fees?
- Is there a cost if you discharge the loan early, make a lump sum repayment, or want to increase your payments?

  This is individual to each loan and may be one of the primary factors in deciding which loan is right for you.

  Often you can't borrow 100% of the price of the home. This means you need to have a deposit saved or in equity in other property – what deposit do you have?
- Which loans will suit my lifestyle and needs?

  As you need a loan and strategy which fits with your lifestyle and income. You need to seek a mortgage broker for answers to these questions.
- Which loans offer the best fixed/ variable rate?
- What flexibility does the home loan offer?
- ATM, redraw facility, credit card, etc.

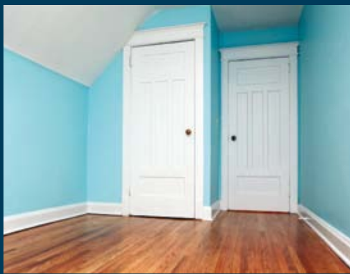
This may seem like a lot of questions to ask about a loan. Keep in mind this is a huge financial decision and responsibility, and you want to have the best information to make up your mind. A qualified mortgage professional can give you all these answers. Don't decide on any loan product until you know the answers to these questions.

7 More Services Offered

The majority of this book has focused on the ability and benefits of a Mortgage Broker to assist you in obtaining a home loan. Although, the majority of brokers' time and business are spent on home loans, they can also help you learn to pay down a loan faster, assist with debt consolidation and give home-buying tips. They also have contacts in the local community that could be of benefit to you when settling in. eg: Lawyers, Electricians, Pest & Building Inspectors, Accountants, Plumbers, etc.

Let's discuss how Mortgage Brokers can teach you to pay down a loan faster. A broker will take a look at your current loan, before doing anything else. It may be time to refinance your loan. Perhaps, you can pay a bit more each month, which will be applied directly to your principal. Lastly, the broker might suggest bi-monthly or fortnightly payments. The most important thing, however, is that your broker will work with you and the lender to find a way to pay the loan down faster.

The next service a broker can provide is debt consolidation. Many people have outstanding debt in a variety of forms; medical, home, car and credit card. Each of these individual debts carry different due dates each month and a distinctive interest rate normally higher than a home loan interest rate. This makes it almost impossible to climb out of the debt hole. A mortgage broker works to get all those debts placed into one spot, with one due date and at one lower interest rate. Once this happens often the weight can be lifted off your shoulders, and you can breathe easier. You are still in debt, but the hole is easier to climb out of – and with assistance you can begin to see the light at the end of the tunnel.



It is important however to address these issues and other debts before you start to have problems meeting payments, as it is much easier and cheaper to refinance credit cards and loans when repayments have been met on time – than a missed payment history.

Finally, mortgage brokers are in the home loan industry which means they know the ins and outs. And this means they have a wealth of experience that they can call on to assist you in buying locally. Sitting down with a broker or having a chat on the phone can give you valuable insights into the entire process and some immediate steps you should take. They can also refer you to other businesses that can assist with your home buying needs.

Mortgage Brokers can assist with:

- Home Loans,
- Investment Loans,
- Commercial Loans,
- Refinancing,
- Plant & Equipment Finance,
- Personal Loans,
- Leasing Finance, and
- Insurance.

Next Steps

The information presented in this book should help you when making your decision.

Buying a home is likely to be the largest financial decision you will make for some time – so you need to get it right.

Making the right choice and putting in place the best strategy to repay it – will also make a huge difference to your quality of life when you retire. This is because the power of compound interest that benefits the banks when you borrow – ends up benefitting you when you pay it off and then deposit those same payments into your future wealth accumulation.

You now know everything there is to know about using a mortgage broker and using a bank to purchase your new loan product. You know how a mortgage broker is committed to maintaining a high ethical standard and also has years of relevant education and service. You also know how the NCCP Act protects consumers by requiring brokers to be licensed.

Mortgage brokers must give excellent customer service to be successful and have access to many more loan options.

You may decide that you want someone to give you more loan choices, personal service and tips on how to pay it back faster. If that is your decision then the choice is clear – head to a mortgage broker and get in touch with our team today.

You may decide that you can educate yourself on what can be a confusing topic, you may have the time and ability to do all the legwork, can get the loan you want locally. You care less about service. If that's the case – head to a bank.

Whatever your decision you have been empowered with knowledge.

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