Home Financing

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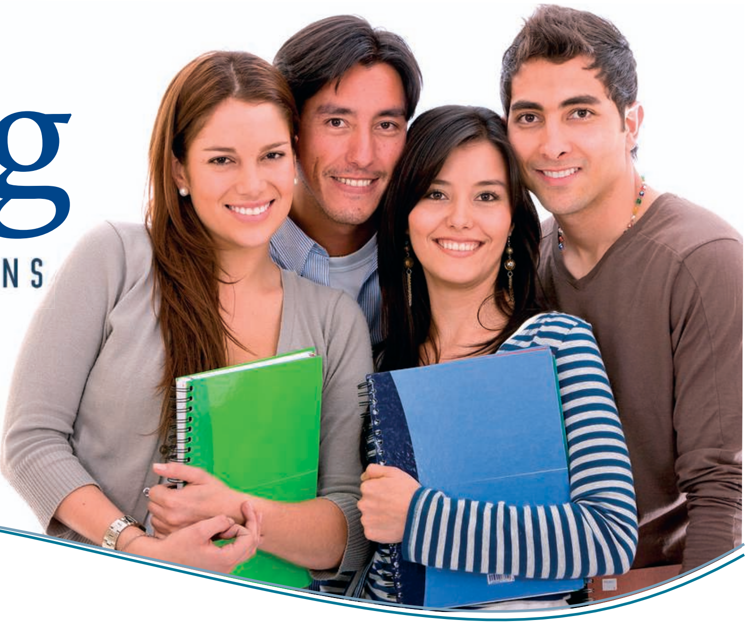

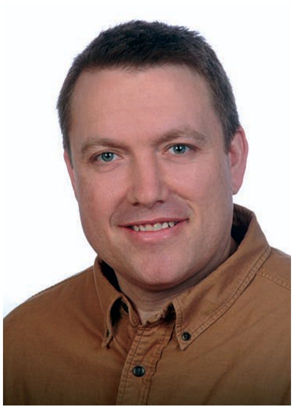

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Another financial year is over and the Global Financial Crisis now seems less like the end of the financial world and more like a standard cyclical contraction (though globally aligned – and fueled by bad US debt). The media seem to have become more and more spectacular in their headlining and appear more interested in selling their products than informing the public and I believe this fed into negative consumer sentiment.

With talk now turning to 'green shoots' in the world wide economy I have noticed lenders in Australia have been quick to lift their fixed rates (on the back of rising investor expectations). My thoughts on variable rates are the Reserve Bank of Australian (RBA) almost never lifts cash rates when unemployment is rising. The government & treasury have forecast rising unemployment till the end of 2010. Given this, I think it's a fair bet the RBA will not be in any rush to lift cash rates any time in the foreseeable future and with rising unemployment may even be tempted to drop cash rates slightly.

Maximising Your Profits from Property

Building long term wealth is very difficult to achieve through salary and savings alone. Learn how to build substantial wealth faster by leveraging your money and investing in real estate using borrowed funds.

Investing in property has long been trusted as the safest means of long term wealth creation. While the stock market certainly works well for many, it can be a volatile and risky roller coaster ride as is currently the case world wide.

Whilst property prices also rise and fall, generally cycles are a lot slower with mild peaks and troughs. Historically figures show that the average property value doubles every 7–10 years.

Property is one of the few investments that allows you to purchase largely with other people's money (i.e. the bank) pay this back with other people's money (i.e. rent) and in many cases enjoy a reduced tax commitment.

So what should you consider before you invest?

Be clear on your goals

This means understanding what you want to achieve from your investment. Is it cash flow, capital gain or both? Are you looking to build a long term nest egg for retirement?

Plan your structure to maximise returns

Consider how your investment should be structured to meet your financial goals. Seek advice regarding tax, type of loans available, repayment terms, cash flow positive investment options and more.

Consider ownership

The actual owner of a property can have significant cash flow and tax implications. For example, whether a couple purchases a property in one or both of their names will impact their legal and financial position.

Your expertise and available time

Are you a first time investor? If so, you may need to seek advice from professionals regarding insurance, financing, flexible structures and minimising bank fees, tax effectiveness, depreciation schedules etc.

Even if you are a professional investor you may or may not have the time to do it all yourself, and so may also need support from professional advisers to help you build your portfolio.

So once you have decided to take the plunge into the property market, how can you make a profit? There are four ways to make money.

1. Passive Appreciation

That's when the value of your property goes up in line with the general property market. Over time, well located properties in Australia double in value every 7–10 years.

2. Active Appreciation

This is when you add value to your property. For example if you buy below market price, or when you renovate or redevelop your property.

3. Rental Return

Rentals from property provide cash flow and rental yields are at their most buoyant in years, driven by low vacancy rates. In some regions, rents are increasing between 5 – 10% as leases expire.

4. Tax Breaks

There are many tax breaks that you are allowed on your investment property. For example, you can claim the cost of two visits a year to your property plus cleaning, gardening, insurance, body corporate fees, etc.

Depreciation also provides you with significant tax breaks where you don't have to spend any extra money. The Tax Office has schedules with rates of depreciation on its website. There are also specialist firms that will assist you to maximise your depreciation claims.

To invest in a top performing property, you need a balance of all four of these elements. Don't focus too strongly on cash flow. This is because well located residential properties are often high growth, low yielding investments.

If you are looking for high yields, perhaps you should consider investing in shares or managed funds. Otherwise be prepared to let your property grow in value over time.

Refinancing

There is one further point to consider – would refinancing your home loan help you to reduce costs?

Competition is keen so you should look around to see if it is worth refinancing. It is important to bear in mind that there are fees and costs associated with switching, which need to be factored in to your calculations.

Get Ahead On Your Debts

Debt consolidation is often portrayed as a way out of trouble.
But for many it's actually a smart way to get debt-free more quickly by reducing the interest being paid.

Many of us have several loans and debts. For example we may have a home loan, a line of credit, car financing, a personal loan, a few credit cards, and some store finance for furniture or renovations. These commitments will all be charged at different interest rates, perhaps with account fees and other charges.

Whilst it may have been logical to set-up and keep these commitments separate, it can mean that you are paying more interest than you have to.

And with the recent dramatic events in global financial markets, many lenders are putting up their rates and fees across many financial products – notwithstanding the recent **RBA** cash rate cuts.

Credit Cards

For example, cards currently have very high interest rates up to 19.99% and higher, with annual fees ranging from $0 to $450, and interest-free days from nil to 62.

Whilst some of the more expensive cards will have rewards and loyalty programs, these may not make up for the differences in interest charges, fees and interest-free days.

Personal loans, car loans and store finance also show wide variations, with some very high interest rates. For example, interest-free finance through a store is an attractive option provided that the debt is cleared within the term. If not, these loans often revert to extremely high interest rates – 20% and higher are not uncommon.

Balance Transfers

The smart way to reduce this debt more quickly is to minimise the interest rate and fees being charged, whilst maintaining the same monthly payment as before.

A good example is to watch out for low interest or even interest-free balance transfers that are regularly offered by credit card providers. You can apply for a new card and then transfer the balances from other credit cards, which will then be charged interest at a very low rate or even interest free, at least for a period of six months and occasionally for the lifetime of the balance transferred.

This can be a good short term solution, but often the interest rate then reverts back to a (comparatively) high rate. So then the whole process of application and balance transfer has to start again.

Also, this doesn't help to reduce the interest rates on some store finance, personal loans and car financing.

Smart Consolidation

A more comprehensive solution is to consolidate all of the debts into a relatively low-interest product such as a home loan. The recent reductions in interest rates on many home loans have made this option look even more attractive.

Consolidation can be done by either using an existing spare capacity, for example using available redraw or an unused line of credit, or by refinancing the entire home loan to borrow a larger amount.

This can often result in more than halving your average interest rates. For example you could refinance a credit card at 18.75% to the standard variable mortgage rate of around 8%. On a debt of $10,000 this represents a reduction in interest of around $1,000 per annum.

Similarly, by refinancing a car loan of $25,000 at, say, 12.75% to a home loan of around 8% you could see interest savings of nearly $1,200 per annum.

Of course in both of these examples the amount of saving would reduce over time as some of the debt principal is paid off, but it would still be substantial.

Now here is an **important point**. By keeping the new consolidated payment the same as the sum of the various payments being made previously, then the debt will reduce more quickly as less interest is being paid, so more of the payment is reducing the debt itself.

Words of Caution

This strategy does work, but you should watch out for the following:

- **Cancel The Old Debts or Cards.** If you transfer the debts (e.g. from credit cards) then you are at risk of building up new debt in its place, which isn't the idea. By cancelling the old credit cards and loans this won't happen.
- **Early Repayment Costs.** Some loans may incur a penalty if paid out early, which can negate some of the benefit of refinancing the debt.
- **Establishment Costs.** Organising a top up on your home loan, or refinancing altogether, will incur some costs. Again you should check what these costs are and factor them into your calculations.
- **Secured Debt.** Refinancing personal loans and credit cards using a home loan means that you are converting "unsecured" debt into "secured" debt. In other words, if you became unable to pay the home loan then you would put your home at risk.

Conclusion

If used correctly and by keeping the new payment at the same level as the sum of the old payments, then using your home loan to consolidate your debts is a good way of reducing interest and clearing personal loans and credit card debts more quickly.

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