

# A COOLER WIND IS BLOWING

## - Allistar Walker

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Many borrowers with mortgages are now aware that the warm, sunny days of low interest rates are coming to an end. The Reserve Bank has left its options open for a lift in the Official Cash Rate (OCR) on either 10 June or 29 July. The likely rise is 0.25% which would impact mostly on short-term rates rather than the longer 3 to 5 year fixed rates.

Some people will have noticed that the short-term fixed rates moved upward recently. The problem the banks, and consequently the borrower now face, are higher funding costs from both onshore and offshore to provide for your mortgages. Since the recession overseas investors have tended to keep their money closer rather than seeking higher 'safe' interest rate returns from New Zealand and Australia. Similarly there has been more competition amongst the banks to attract term deposit funds here, as a number of investors have sought the safety of bank deposits rather than finance companies.

The cost of overseas funding is expected to increase as investors tend to be wary of sending their money to highly indebted countries. Our banks, in order to get sufficient to give to borrowers, will need to pay higher interest rates to make investors more willing to part with their dosh. You, the borrower will pay.

### What should a borrower do?

Only floating or the shorter 6 month to 2 year fixed rates offer any value. Your priority whether to fix or float will be dictated by either

- Maximise remaining chances of additional capital reduction by floating (or taking a 6 month fixed) and adopting a higher repayment programme ie We encourage our clients to maintain a repayment programme based on an interest rate of 8% even though they may only be paying 5.95%. By doing this, regardless of whether fixing or floating you will be ahead of the ball game when interest rates go higher.
- Hedging your risk by taking a fixed rate or a combination of fixed rates and floating rates eg fix some for 6 month and some for 2 years and float some you wish to kill off quickly.

The longer the RBNZ maintains the current OCR (2.5%), the more attractive the floating rate would turn out to be. Unfortunately one has to make a call before the ball starts rolling. No one, not even Mr Bollard (RBNZ), has a crystal ball.

### Some hints to help

Over the last 30 years mortgage rates have averaged a little over 7.5%. Over the last 10 more turbulent years, mortgage rates have averaged 7.5% (6 month fixed) and 8% (5 year fixed). Current short term rates (0-2 years) as you can see are well below longer term averages. When interest rates all dropped below 7%, there was the golden window for fixing as long as possible. When the rates were in the upper 8% into 9%'s, that was and will be in future the time to fix short, or float, so you can take advantage of lower rates when they drop, as they eventually do. Now may be a time to float up through the highs or fix short and wait for the next bottom cycle.

The OCR is expected to go to around 4% by early 2011. That would translate to floating mortgage rates of 7.25% to 7.5%. Floating rates could further rise from between 8% to 9% by mid 2012. Hopefully it may be lower, but planning should take into account worst case scenarios.

### Advisors Can Help

Everybody's situation is different and like many Mortgage Advisors our planning service is designed to accommodate individuals or business entities particular goals and objectives, utilising up to date data. Our contact details are below.

*Care has been taken to ensure that any information is accurate. No liability is accepted for its use.*

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