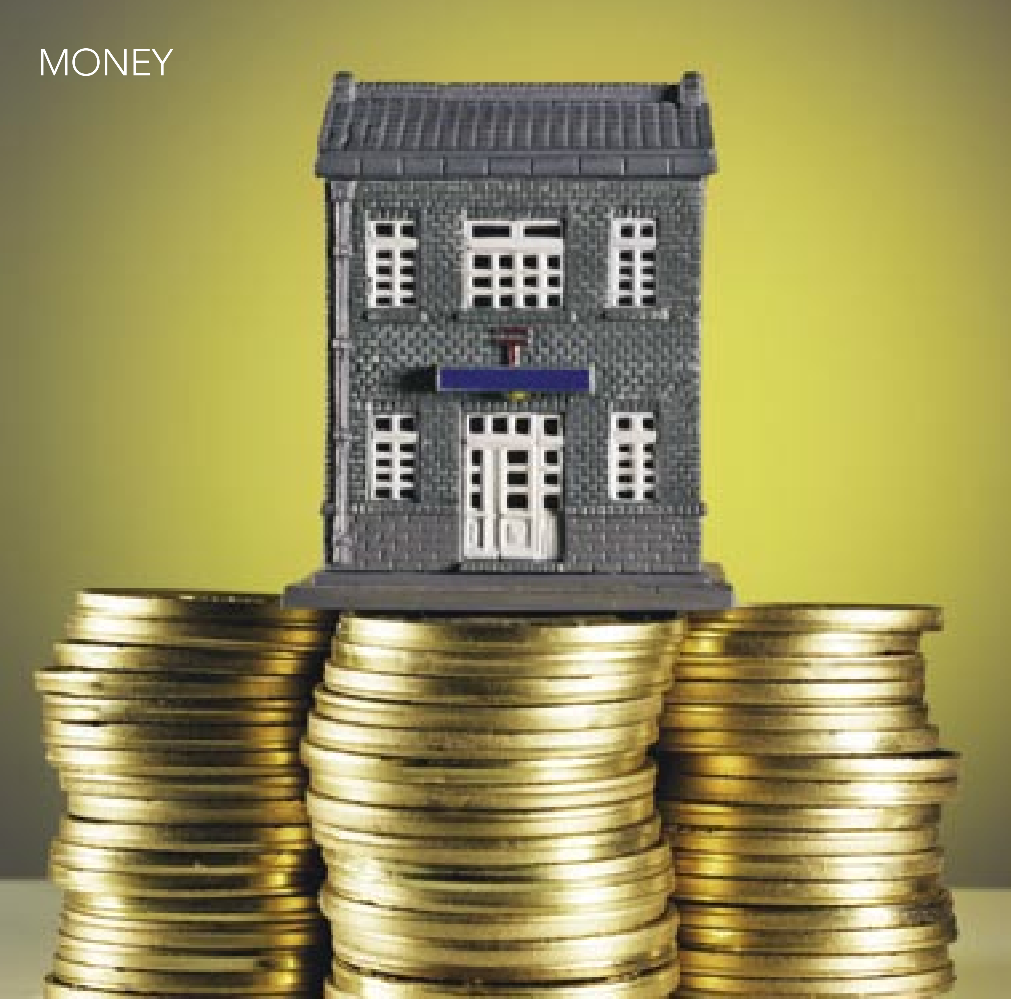

Your best interests

It's tempting, but breaking your mortgage term might cost more than it saves, says Finance Editor Susanna Stuart

OVER THE PAST few months, New Zealanders have witnessed a real plunge in bank lending rates – now they've eased back to about 6% or less. This is good news for some, but not so good for others.

If you have a floating mortgage rate you'll have felt the easing off, either through a lower repayment obligation or through the satisfaction of knocking a lot more off the principal owing each month than you used to. Feels good, doesn't it?

But alas, many New Zealanders are on fixed rates – fixed back when it looked as if rates might climb. They're still paying about 9% and are feeling hard done by. Is it worth renegotiating for a lower rate and swallowing the bitter pill of an early repayment charge, known as a break fee? The calculation depends on five factors:

- **Your bank**. Banks use different formulas for calculating break fees.
- **Your mortgage terms**. Are you locked in at 8% or 9%?
- **The current rates.** They change daily.
- **The length of your fixed-rate mortgage term.** For example, if you have four years left fixed at 9% the break fee will be much higher than just one year fixed remaining.
- **Interest rates.** Whether today's low interest rates will still be around if you wait.

If you have a fixed-rate mortgage it will be tempting to refinance your mortgage and incur a break fee to have the certainty of a low rate for five years.

I've seen a couple of online repayment calculators that help you work out the arithmetic, but they don't do it very well because of the unique aspects of just about every mortgage.

I suggest you see your bank manager or senior lending officer to do the maths for you before making any decisions. For most people on a fixed mortgage this bank visit could result in a saving of several hundreds, even several thousands, of dollars over the next five years. While you're at the bank:

- Get in writing what the break fee will be and how they make their calculations.
- Ask if they charge an administration fee. This can be $250 or more.
- Consider whether you can add the break fee to the new loan.
- Ask the bank to calculate the time it will take before a mortgage at a new, lower rate – break fee included – will put you ahead of your current situation. It might take a couple of years or more.

Now you have the information you need to make decisions. Remember, today's low and very advantageous mortgage rates won't last forever – some analysts say they may begin to rise again after September. In the end, your decision will be largely based on your view of where the rates will be one or two years from now. In this jumpy market not many are willing to make a prediction.

But those lucky people with floating rate mortgages might consider this: With little room to go down, and plenty of room to climb up, it might be worth locking your mortgage in at today's attractive rates.

What if you're in the fortunate position of having surplus savings? With interest rates so low, should you use the money to repay the mortgage first or should you invest?

I advise reducing the mortgage as this is a low-risk strategy. If you want to invest you'll need to earn a return after tax that is higher than the mortgage rate. Investing in shares can provide potentially higher returns but these can vary hugely at times and you need to be comfortable with risk.

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