Fixed Rate Home Loans

Farmer does Finance

A fixed rate home loan allows you to set your interest rate for a period of time. This is usually in the range of one to five years. Sometimes, you can arrange to secure your interest rate for longer.

Fixing your interest rate can be a suitable option for some people, however you should be aware of the following:

- Fixed rate home loans often have higher interest rates than variable rate home loans. Often, the longer the fixed rate term, the higher the interest rate is likely to be. For example, a five-year fixed loan will usually have a higher rate than a three-year fixed loan.
- If interest rates do not rise, or if they fall during your fixed rate period, you could then pay more interest than you would if you had a variable rate home loan.

What's good about fixed rate home loans?

- During times of low interest rates, locking in a fixed rate could work to your advantage, because you can retain a low rate for a fixed term even if the rates rise steeply. Depending on the lender and the current interest rate, this could potentially lower your repayments and the total interest paid over the loan term.
- You know exactly how much your repayments will be during your fixed rate term, which can make budgeting easier.

Things to consider

- **Less Flexibility.** Fixed rate loans usually do not have the same flexibility that a variable rate loan provides. For example, you may not be able to make extra repayments and un turn redraw the extra amount paid into the loan. Some lenders do allow extra repayments to be made but will restrict the extra amount that can be paid during the fixed term or on an annual basis.
- **No offset facilities.** Most lenders will not allow you to have an offset account with a fixed rate loan so there is no opportunity to save on interest. Where offset facilities are available, they will usually only be available on a partial basis, with a 100% offset account being available through some lenders only.
- **Break costs.** The decision to break your fixed rate loan is entirely up to you however a break cost may be applicable. Break costs may apply if:
    - you want to exit before the end of the fixed term.
    - you prepay part of or your entire loan before the end of your fixed rate period
    - you switch to another product, interest rate or payment type before the end of your fixed rate period.
    - you want to end the loan as part of selling the property.
- **Calculating break costs.** Each bank uses a different formula to work out the break costs, so it's worth finding out how your lender calculates this fee as the formula is complex. However, in general terms if the current wholesale interest rate for the remaining part of the fixed interest term is lower than the original wholesale interest rate when the fixed interest rate period started, then a Break Cost will be charged.

The rate is usually not set until settlement. Some lenders will apply the fixed rate at the loan settlement date or the date the fixed rate period commences while others will apply the fixed rate available at the time you sign your letter of offer. This may or may not work in your favour. There may be an option to lock in your fixed rate (see below), however there might be a fee from the lender for this.

- Your decision whether to fix the interest rate on your loan should be based on your own circumstances, with your future in mind. Certainty of repayments is the best reason to fix your rate—they seldom help to beat rate rises over time.

Remember:

If variable rates increase, you may pay **more** interest than if you fix your rate. It will depend on the size of the increase(s), how far into the term the increase(s) occur, and how long you hold the loan after the increase(s) occur.

If variable rates stay flat or decrease, you will pay **less** interest than if you fix your rate. This is on the basis that your fixed rate is higher than the variable rate over the same period.

Rate Lock

Some lenders will provide you with the option of locking in the fixed rate prior to settlement occurring. This is referred to as “Rate Lock” and will involve paying a rate lock fee which will usually be calculated as a percentage of the loan amount.

This fee can be a significant amount, although some lenders will not charge a fee or may waive it. If you choose this option, then you can proceed with certainty and complete peace of mind that the decision to fix your interest rate will not move between when the rate lock is effective and the rate that would be applicable on the day of settlement.

Most people who elect to Rate Lock do so at the time the application is submitted. It can be done later in the process— however, the lender can announce a rate increase at any time before settlement and once announced the opportunity to lock in the previous rate passes. A “wait and see” approach carries with it the risk of missing out on the lowest fixed rate that could have been obtained.

If you decide to Rate Lock, make a note of the expiry date, as it will usually be in place for 90 days. If your settlement still hasn’t occurred when it expires, it will need to be renewed (including paying another fee) for it to remain in place. This can be an important consideration if you have negotiated a long settlement.