



Feel happy with your home loan

What types of home loans are available?

There are many types of loans to choose from. Here's a guide to the most common loans available.

Variable Rate (Principal and Interest) Home Loan

This is the most common loan type in Australia. The interest rate charged on the loan increases or decreases in accordance with movements in interest rates, as set by the Reserve Bank.

Advantages:

- Repayments fall when official interest rates fall
- Flexibility and additional loan features, such as the ability to make additional payments, redraw facility (take out any extra money that you have put in), low honeymoon rates
- Allows for paying off the mortgage quickly with no penalty for early payout of the loan if circumstances change

Disadvantages:

- Interest rate is higher for standard variable loans than basic loans because they usually offer additional features
- Repayments rise when official interest rates rise
- Offer less budgeting certainty than fixed interest rate loans as repayments can change

Basic or 'no-frills' Home Loan

These loans usually offer only limited features, such as only standard repayments, no offset account etc., for borrowers that simply wish to pay off the standard loan amount each period for the life of the loan. You often have the option to pay for any additional loan feature required.

Advantages:

- Usually offer a lower interest rate than variable loans

Disadvantages:

- Less flexibility and fewer loan features, such as redraw facilities or no extra payments
- No option to pay the loan out early if circumstances change

Fixed Rate (Principal and Interest) Home Loan

A loan type provides a fixed interest rate (and loan repayment amount) for a period of the loan (usually between one and five years). The longer the fixed rate selected, usually the higher the interest rate. Once the fixed rate time period expires, the borrower can then choose to either 'lock-in' for another period of time at whatever the fixed rates are at that time, or revert to the current variable interest rate.

Advantages:

- Repayments do not rise if the official interest rate rises
- Provides peace of mind that a borrower will not be effected if interest rates rise during the fixed period
- Budgeting can be easier with fixed loan repayments

Disadvantages:

- If variable interest rates fall, fixed rate repayments do not
- Only limited additional payments are permitted
- Penalises early payout of the loan, limiting the benefits available from refinancing to a better deal

Split Rate Home Loan

A split rate loan has one portion of the loan fixed and one portion variable. You can choose which amount is allocated to each type of loan structure.

Advantages:

- Provides some peace of mind about possible rate rises
- More certainty in budgeting is achieved than with a full variable home loan
- Additional payments can be made on the variable loan component

Disadvantages:

- Additional payments are limited
- Repayments will rise with rate rises

Capped Rate Home Loan

This loan type is similar to a variable home loan, in that interest rates can rise with movements in the money market, although the rate rise is capped at a certain level

Advantages:

- Some peace of mind is achieved, as borrowers know the maximum rate that the interest rate can increase to for a fixed time period
- More certainty in budgeting than full variable rate loans
- Although the rate is capped to a maximum level, the rate can also reduce with falls in the money market

Disadvantages:

- Interest rates are often slightly higher than variable home loan rates

100% Offset Home Loan

With this loan type, all salary and other income is paid directly into an offset account that is directly linked to your home loan. Any balance in the offset account is 100% 'offset' against your home loan. This reduces the amount of interest you have to repay, making your money work harder for you.

Advantages:

- You can save a significant amount of interest if used correctly
- Operates like a normal transaction account and has a chequebook, ATM card etc. attached

Disadvantages:

- May have higher monthly fees attached to the account
- May require a minimum balance in the account

Interest-Only Home Loan

This type of loan can be very suitable for property investors, or if you require funds to renovate. It is only necessary to pay the interest on the principal amount during the interest-only term of the loan, (this is usually between one and five years), so repayments are lower than with a standard principal and interest loan. You must then start making Principal and Interest Repayments over the remaining term of the loan.

Advantages:

- Lower repayments initially so you have more money to renovate
- This loan type may make an investment property more affordable in the short term

Disadvantages:

- Repayments will increase suddenly at the end of the Interest Only period
- Your full borrowing power may be limited, as lenders approve the loan based only on your ability to repay the principal and interest amount, even though you will initially only have to pay interest

Line of Credit Home Loan

The equity in your property can be accessed, up to an agreed amount per month, when funds are needed. A minimum loan repayment amount must be paid each month, and access to some funds is then available at a home loan interest rate, rather than higher personal loan or credit card interest rates.

Using the equity in your own home can also be a clever way to access funds to purchase an investment property.

Advantages:

- Home loan interest rates tend to be lower than credit cards or personal loans
- Offers flexibility

Disadvantages:

- Potential for a reduction in the equity in your residential property
- Usually higher interest rates than some other home loans
- Can be very expensive if not used carefully

Low-Doc or No-Doc Home Loan

These loans are available to borrowers who may have access to less financial reports, such as self-employed or property investment borrowers. Limited tax returns or financial reports are required.

Advantages:

- Simple income declaration form
- Limited tax returns or financial records required
- Full loan flexibility, with loan features such as redraws, line of credit, variable or fixed rates
- Borrowers have the option to take out a Principal & Interest or Interest-only loan

Disadvantages:

- In exchange for potentially higher risk for the lender, you are usually charged a higher interest rate

Honeymoon Rate (or Introductory Rate) Home Loan

Borrowers can enjoy a lower interest rate on this loan, either as a fixed or capped rate, usually for the first 12 months, before the rate then rises to the standard variable rate.

Advantages:

- Usually the lowest available rates
- When payments are made at the introductory rate, the principal can be reduced more quickly
- An offset account is available with some lenders on a honeymoon rate loan, allowing you to reduce your interest payments even further

Disadvantages:

- Payments usually increase after the introductory period

Non-Conforming Home Loan

It can sometimes be difficult to secure a home loan if you have a poor credit rating. In this situation, many lenders offer a 'non-conforming home loan'. However, in exchange for securing a home loan when in this situation, you are likely to be charged a higher interest rate, and may also need a larger deposit to secure the loan.

Advantages:

- It is possible to secure a loan even with a poor credit rating

Disadvantages:

- A higher interest rate is usually charged than other loans, and a higher deposit may be needed

Construction Home Loan

If you are building your own home or investment property, a construction loan may be suitable for you. This loan requires a fixed price building contract from a registered builder. These loans are usually interest only for the period of building and then become principal and interest once building is completed. A construction loan allows you to draw money as is required whilst building. As well as the usual necessary documents required when applying for a loan, construction loans also require a 'fixed price building contract' and 'council approved plans'.

Advantages:

- Competitive variable interest rates
- Facility to draw money when necessary whilst building
- Interest only payments during the building period
- Additional payments can be made

Disadvantages:

- Requires a fixed price building contract leaving little room for change whilst building
- Some lenders charge a fee for every time you draw money whilst building
- Loan repayments will increase if interest rates go up

This information is intended as a quick summary only of the different types of home loans available. Please contact us for more information on the loan types that are most suitable to your individual needs.