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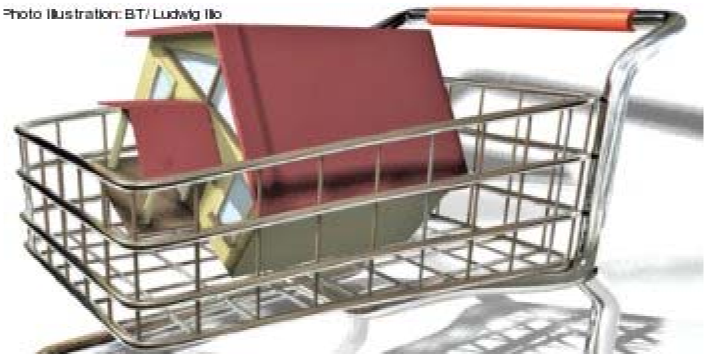
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Don't overpay for your home loan

WHAT interest rate are you paying on your housing loan? If you are paying 3.5 per cent or more, you might be overpaying. With the US Federal Reserve cutting interest rates, the Singapore Inter-bank Offered Rate, or Sibor, has been on a downward trend. Sibor is the rate at which banks lend to one another. Currently, the three-month Sibor has fallen to about 1.4 per cent, down from about 2.5 per cent last year.

Banks have started lowering interest rates offered on housing loans to as low as 2.08 per cent. Thus, if you're paying an interest rate of 3.5 per cent or more, it might make sense for you to refinance your housing loan to enjoy interest savings.

For example, if your outstanding loan is $500,000 and you're currently paying 3.5 per cent interest with a remaining loan period of 20 years, the total interest savings for the next three years from refinancing can work out to $13,831.38. After factoring in the cost of refinancing, the net interest saving still works out to $13,331.38. Thus, by refinancing, you can be 'richer' by over $10,000.

If consumers hold the view that interest rates are likely to fall, choosing a housing loan package pegged to Sibor would enable them to automatically enjoy lower interest rates as Sibor moves lower.

Floating rate vs Sibor/SOR pegged packages: Each bank will usually set its own board rate and after deducting a 'discount factor', arrive at the floating (adjustable) interest rate charged to clients. The problem is that each bank will set its own board rate arbitrarily and there might be occasions when Sibor rates fall, and banks don't reduce the interest rates charged on floating (adjustable) rate packages. Thus, in a bid to increase the transparency, some banks have recently introduced housing loan packages with interest rates pegged to Sibor or Swap Offer Rates (SOR).

The advantage of such packages is that as and when inter-bank offer rates move up or down, your interest rate would be adjusted as well - it would not be at the bank's discretion. Currently, Sibor/SOR have fallen below 1.4 per cent and interest rates charged on such loans can be as low as 2.08 per cent.

With the US expected to continue cutting interest rates in the next few months, Sibor is expected to remain low or even fall further in the next six to 12 months. Thus, if consumers hold the view that interest rates are likely to fall, choosing a housing loan package pegged to Sibor would enable them to automatically enjoy lower interest rates as Sibor moves lower.

Beware: Fixed rate packages typically come with lock-in periods. Some banks recently also adjusted interest rates charged on their fixed rate packages downwards to an average of 2.58 per cent for the first three years. However, such packages come with a penalty period of three years. Thus, such packages might not be suitable for consumers who intend to sell their property within the next three years, as they are liable to a penalty fee.

Should you apply for a housing loan now for properties purchased on a deferred payment scheme? You might have purchased a property on a deferred payment scheme and only need to take a loan when the project gets its Temporary Occupation Permit (TOP), which might be in 2009 or 2010. Should you apply for a housing loan now?

By applying for a loan now, you eliminate the risk of loan rejection should there be any adverse change in your financial situation in future, for instance, a pay cut or job loss when the property is ready. You also eliminate the risk of banks granting a lower loan quantum should the property market turn and prices fall. To safeguard your interests, you can choose a loan package that allows you a free loan conversion so that you can switch to a better package should one be available nearer TOP.

Cash in on your property without selling it: With property prices having gone up in the past three years, you might now own a property whose value has doubled. In that case, your current debt-to-asset ratio might have fallen considerably.

For instance, say you bought a $1 million property three years ago and took an 80 per cent loan, or $800,000. Currently, the loan outstanding is about $750,000, while the current value of this property might have gone up to $2 million. This means your current debt-to-asset ratio is only 37.5 per cent.

How can you benefit from the rise in the property price without selling your property? You can consider taking an equity loan on the property. For instance, in the above example, subject to your credit score, banks might grant you an additional equity loan of up to $850,000. To be conservative, you can consider taking up a lower equity loan of, say, $450,000, bringing your debt-to-asset ratio to a comfortable 60 per cent. You can use the $450,000 equity loan granted by the bank to start a business, or even to invest in another property. The interest rate on equity loans in Singapore is very low and can be as low as 2.2 per cent currently.

Should you pay off or reduce your housing loan?: The Singapore government has projected the inflation rate in 2008 to be about 5 per cent. On the other hand, the interest rate on housing loans is about 2.2 per cent. Thus, we have a rare scenario of negative interest rates, that is, a person who takes a housing loan is actually ahead of someone who saves money in bank deposits because of the shrinkage of money from inflation.

On the other hand, interest rates on bank deposits have fallen to about 1.5 per cent. With inflation at 5 per cent, it means that a consumer is losing 3.5 per cent a year by putting money in bank deposits.

Instead of paying down your housing loan which charges low interest rates of less than 3 per cent, you can consider investing your cash in a stable investment that is not subject to large price fluctuations and offers higher returns than fixed deposits. One example is UK-traded endowments, which have a guaranteed cash value and generate annual returns of 6-8 per cent.

How to choose a suitable housing loan?: There are over 113 different housing loan packages available in Singapore at any one time. Each package has its own unique features, with its own pros and cons and different terms and conditions. Consumers might be confused by the wide array of choices. In the last few years, with the emergence of independent mortgage brokers in Singapore, home loan shopping and comparison have been made easier.

Basically, an independent mortgage broker who knows your requirements can help you zoom in on the most attractive home loan packages suitable to your needs. You typically do not have to pay for the service of a mortgage broker as banks pay them a fee.

In more advanced countries such as the US and Australia, people usually apply for home loans through a mortgage broker rather than go to the bank directly. In Singapore, many people are still unaware of the services and benefits of engaging a mortgage broker, but things are likely to change with public education and increasing awareness.

Dennis Ng is a Certified Financial Planner with 15 years of experience in bank lending. He co-founded an independent mortgage consultancy portal www.HousingLoanSG.com in 2003.