

OCTOBER 2017

NEWSLETTER

INVESTMENT LOANS ARE HARDER TO GET – WE MAKE IT EASY!

Investors are aware that their loans now attract higher interest rates than home loans and most are aware that the banks are also restricting the LVR or Loan to Valuation Ratios for Investment Loans. What is less obvious is that banks are also applying tighter assessment guidelines when assessing the applicant's loan servicing capacity, or in simple terms, their ability to make the loan repayments when all of their income and expenses are considered.

This is leading to confusion and frustration for many applicants who know they can afford the loan, based on the money going in and out of their bank account. At M Point it is our business to understand the various nuances of each lender in regards to investment loans. It is clear some lenders are underweight investment loans and are not as restrictive. Below we outline some of the recent changes and how lenders now assess the capacity of Investors to repay their required loan.

RENTAL INCOME – When assessing an applicant's rental income, lenders do not use the full gross rental income figure. That figure is instead discounted to allow for vacancies and the costs associated with the investment property. Commonly a discount of 20% is applied to the gross figure (some lenders apply an even greater percentage) meaning that when the bank looks at an applicant with \$500 per week rental income, they will only use \$400 in their servicing assessment, wiping \$5,200 per annum from their assessable income. The more properties held and the more rental income the applicant relies on, the more impact this has on their cash flow forecast and the more difficult it is to pass the

assessment.

LOAN REPAYMENT CALCULATIONS - All loans are now assessed using a 'stress interest rate' that is much higher than the actual interest rate applied to the loan. Typically, this is around 7.50% and is used to assess future loan repayments. This is also applied to any other loans the applicant may have. In some cases, these rates are almost double the actual rate being charged. This is done to allow for potential rate rises over the life of the loan. The outcome is that all of the assessed loan repayments for the applicant are significantly higher than the repayments the applicant is actually making, increasing the expense figure in the banks servicing calculations. So now the applicant is faced with the income figure used being reduced and the expense figure inflated. Again, the more properties and borrowings the applicant has, the more the impact on their ability to obtain a loan.

INTEREST ONLY REPAYMENTS – A little known but very significant shift in the assessment process has been in the way banks treat interest only repayments. Previously, interest only repayments were included in the assessment at the actual repayment figure. No consideration was given to repayment of the loan principal or the significant lift in repayment amount when the repayments reverted to principal and Interest repayments at the expiry of the interest only period – repayment shock. To cater for that outcome, not only is the 'stress rate' applied to the interest rate calculation but the repayments are based on the principal and interest amount that will be applied when the repayments come off the interest only period. This makes a huge difference to the expense calculations of the applicant.

LIVING EXPENSES - This has recently been a focus of the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC) with the lenders again responding to pressure from these bodies. Prior to the spotlight being shone on this issue, lenders commonly applied a benchmark living expense figure to their calculations for simplicity but these have now evolved to more detailed calculations depending upon individual applicant circumstances such as location and income. The lender will also ask the applicant to provide an estimate of their living expenses. This figure is compared to the benchmark established by the lender and the higher of the two is used in the calculations. This has led to a marked increase in the expense figure of a large number of applicants. So again, this application of policy has led to a negative impact on the applicants borrowing capacity via an increase in the expense figure.

These are just a sample of the factors that have impacted the capacity of investors to obtain loans. Add to these the increased rigor of verification of the information provided by applicants, higher property values in Melbourne and Sydney, the scaling back of assessed gearing benefits and it is clear why it is more difficult for investors to borrow now than just a few short years ago (despite what some in the press claim). Although frustrating for many, in the main the changes provide additional protection for investors and they have certainly contributed to the slowing of investment borrowings. If you're unsure of your borrowing capacity or how the changes affect you, talk to us here at M Point Finance. We are dealing with many different scenarios and using our expert knowledge we are able to match the appropriate lender to each investor's needs.

Important: Clients should not act solely on the basis of the material contained in the newsletter. Items herein are general comments only and do not constitute or convey advice per se. Also changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. Newsletters are issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and not be made available to any person without our prior approval.

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