Heat on mortgage holders

By NZ Herald Andrew Koubaridis Friday Mar 14, 2014

Experts warn homeowners to get finances in order as interest rate rises start to bite.

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Homeowners are being warned to prepare for harder times as the days of low interest rates come to an end.

The Reserve Bank yesterday lifted the official cash rate (OCR) from 2.5 per cent to 2.75 per cent, a move that will increase mortgage payments - and for many Kiwis should be a "wake-up call" to get their finances in order.

The OCR is expected to rise by 1 per cent by September, including yesterday's 0.25 per cent hike, triggering mortgage interest rate rises.

Every percentage point increase is going to cost homeowners about $20 a week for every $100,000 owed to the bank. For a $400,000 mortgage, that's an extra $80 a week.

Shamubeel Eaqub, principal economist at the New Zealand Institute of Economic Research, said interest rates were set to rise by about 2 per cent over the next year or so.

"The context is they are rising from historically quite low levels and what we are talking about is interest rates going back to more normal levels."

That could see floating mortgage rates getting towards the 7.5 per cent mark.

He said people who had floating mortgage rates or fixed rates that were due for renewal needed to think very hard about what the interest rate increases would mean for them.

The immediate impact was not major but over the coming months, as each rise in the OCR nudged up interest rates, the cost would become more noticeable.

Mr Eaqub said there were a number of possible responses.

"You could fix your mortgage to give you some time to plan for higher interest rates; that buys you a bit of breathing room. In the recession, when things were getting difficult, a lot of borrowers extended their mortgage terms. It's fine to do that, but over the life of the mortgage you will pay more in interest - and it will turn out more expensive."

So households were faced with making some important decisions.

Mr Eaqub's advice was to plan for at least a 7.5 per cent interest rate over the life of the mortgage.

"Quite often we buy houses on emotion rather than logic. Rising interest rates should be a wake-up call to get finances in order. You don't want to wake up in a year's time to find yourself in financial difficulty."

ASB economist Christina Leung said there had been warnings of interest rate rises for some time and more were coming.

"People have to ... budget for that."

Despite that, Ms Leung didn't think it would mean a return to the very high interest rates of the past.

"The Reserve Bank highlighted [yesterday that] one of the uncertainties is how households' behaviours will change given the tightening cycle has now started, so that is a key uncertainty."

The chief executive of the New Zealand Federation of Budgeting Services, Raewyn Fox, said it would be especially hard for young families who got their first mortgages in times of low interest rates.

Mrs Fox said it was a very real possibility that people would "come unstuck if they hadn't thought ahead".

She advised people to start rewriting their budgets now before it was too late.

"One of the key things you need to be really aware of is not taking on any more commitment or credit or anything, knowing that if you take something on now it may not be affordable."

- NZ Herald