MORTGAGE STREET

Guide to Buying your first Home

MSt **028**

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The Mortgage Street guide to buying your first home

Buying your first home will be one of the most rewarding and challenging purchases of your life. It is an incredibly stressful time and one of the biggest financial decisions you will have to make. Understandably, you will need all the support you can get from friends, family and professionals. We're not going to lie; you are in for quite the emotional rollercoaster. You can expect some big ups and downs, but in the end, you will achieve the sense of happiness and security of owning your own home.

At Mortgage Street, we spoke to a number of our first home buying clients. They gave us valuable insight and advice on how they managed the emotional side of the purchasing process and what they would do differently if they could go through it again. From this information we have put together a step-by-step guide to help prepare you for the long and sometimes bumpy road ahead.

When did you decide to buy a home?

If you are thinking about buying your first home, chances are you have a few friends in the same situation. You probably noticed your friends had started talking about open homes, auctions and home loans at BBQ's and get togethers. Maybe you are getting married, or maybe you are sick of living in share houses and tired of renting. Whatever the reason, you have come to the decision you are ready to own your own home – and that's great. You've probably also come to the realisation that you have got absolutely no idea how to go about it.

No one expects you to be an expert

When buying your first home, you will come across a range of terms and forms that you may have never seen or heard of before. Even if you have heard of them you may not fully understand what they mean.

One of the most important things to realise is that it is okay to admit when you don't understand or need clarification. You will be bombarded with an incredible amount of complex information. No one expects you to be an expert. So don't be afraid to ask questions, no matter how silly they may seem. It's your home buying journey, you need to feel comfortable and in control from the very beginning.

OMG what's an LVR? Let's start with the lingo

You are worried about paying LMI, you need to make sure you get a LVR and you have very little idea what any of it means. Below is a breakdown of the terms you'll come across during the home buying process.

Fixed Rate Home Loan:

A Fixed interest rate home loan is usually taken out for an agreed period of time between 1 and 5 years. When this ends, you have the choice of fixing the rate again or switching to a variable interest rate. Your repayments will remain constant during the fixed term, regardless of any interest rate changes.

Progressive Fixed Rate Home Loan:

This loan is similar to a standard Fixed rate home loan, with the exception that it has the ability to make extra mortgage repayments without incurring a penalty fee. Progressive Fixed rate loans generally offer more flexibility and include additional features such as a redraw facility and an offset account.

Offset Account:

Using an offset account allows you to potentially save time and money off your mortgage simply by using your regular income. By placing any income you receive into the offset account you only pay interest on the balance of your home loan account minus that of your offset account. For example if you have a $150,000 mortgage and there is $5,000 in your offset account you will pay interest on $145,000, meaning the more in your offset account the more you save.

Variable Rate Home Loan:

A Variable interest rate home loan is subject to changes in interest rates. If the interest rate rises, so will your repayments. However, if the interest rates decline, your repayments will also be reduced. Where as with a Fixed rate loan, if interest rates fall, the home loan repayment will not reduce as your repayment amount always stays the same.

Loan to Value Ratio (LVR):

The loan to value ratio refers to the proportion of money you borrow compared to the value of the property.

E.g. Purchase Price $600,000 with a loan of $570,000 would be a LVR of 95%

Lenders Mortgage Insurance (LMI):

Generally if you borrow more than 80% of the property's value, you will have to pay Lender's Mortgage Insurance (LMI) adding additional costs to the purchase of a home. This insurance benefits the lender and protects them in the event that you default on the loan.

While Lender's Mortgage Insurance might seem like just another cost, you could look at it as the cheapest insurance you will ever pay for, as it will provide the biggest return on investment.
If you have a small deposit and you want to avoid paying Lender's Mortgage Insurance, it might take you another five years to save up for a deposit. In that time the property value of a house you could have purchased would have increased by around 18%. This means that on a $600,000 property you will have missed out on $108,000 in capital growth on the property over the five years.

So depending on how long it takes you to save, Lender's Mortgage Insurance can allow you to enter the property market earlier and provide a larger return on your investment in the long run.

Lenders Mortgage Insurance is cheaper because it locks down current prices, protecting you from price rises, no increase in Government Stamp duty due to prices increases.

Stamp Duty:

Stamp Duty covers the cost of the legal documents for the transaction. It is a tax charged by the government on the sale of the property. The tax is different depending on which state you live in. In NSW Stamp Duty is required to be paid three months after exchange of contracts or on settlement, whichever is earlier. Stamp Duty is calculated on the dutiable value of the property, which is the higher of the purchase price and the current market value. Stamp Duty in NSW is around:

$18,000 on a $500,000 purchase

$36,000 on a $900,000 purchase

$68,000 on a $1.5m purchase

x$95,500 on a $2m purchase

Interest Rate:

The interest rate is the rate charged by the lender to the borrower for the use of the money loaned. It is usually expressed as an annual percentage of the principal amount.

Comparison Rate:

A comparison rate helps customers work out the true value of a loan. It is worked out by looking at the amount of the loan, the term of the loan, the repayment frequency, the interest rate and any fees and charges connected with the loan. It displays a single percentage rate that can be used to compare various loans from different lenders.

First Home Owners Grant (FHOG):

The First Home Owners Grant scheme was first established to offset the effect of the GST on home ownership. Under the scheme, a one-off grant is payable to first home owners that satisfy all the eligibility criteria. The grant varies from state to state similar to Stamp Duty. In NSW a $15,000 grant applies for new homes only & reduces to $10,000 on 1 January 2016. For a full list of grant information & conditions for each state please visit www.firsthome.gov.au or please contact your broker to find out more & to find out if you are eligible for this grant.

Borrowing Calculator:

Positively geared properties are when the rental return is higher than your loan repayments and outgoings. Positive cash flow properties are self-funding and are considered to be a conservative investment strategy that provides an income with exposure to the prospect of capital growth. Keep in mind that with positive gearing there is the potential that tax will be payable on the net income (after the consideration of depreciation and other tax deductions).

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Negative Gearing:

Negatively geared properties are when the rental return is less than your loan repayments and outgoings (placing you in an income loss position). There is however the underlying expectation that the accumulated losses will be more than offset by the capital growth on the property. The key benefit associated with negative gearing is that the loss associated with the property ownership can be offset against other income earned, reducing your assessable tax income, thereby reducing your tax payable.

Legal fees:

First homebuyers are often shocked at the number of expenses involved in buying a property, from legal and bank fees to government charges, the costs add up. As a general rule, you should budget for around 5-10% of the purchase price to be spent on acquisition expenses. These costs vary, but the following checklist covers most of the common expenses:

Type of cost	Cost
Valuation fees	$200–450
Conveyancing fees	$1,000–2,000
Lender's solicitor's fees	$250
Loan application fee	$300–600
Annual package fee	$400
Stamp or transfer duty	Concessions often apply for first home buyers – otherwise, can cost upto 5% of the purchase price
Lender's mortgage insurance	Varies - it is charged on all mortgages when the loan to value ratio is higher than 80% Mortgage Stamp Duty Varies - not applicable in all
Mortgage Stamp Duty	Varies - not applicable in all states and territories, and is directly proportional to the size of your loan
Government charges (registration of transfer of land, registration of mortgage etc.)	$500-1,500

GUIDE ONLY

Mortgage Registration Fee:

This is a government fee paid when a mortgage is established against a property. The Land Titles office in each state or territory collects the fee for registering the lenders mortgage on the title record for the property.

Searches:

When you buy a property, you buy it within a Torrens title system. The Torrens title system guarantees you the title and ownership of your property and ensures that no one can displace you. During this phase, your solicitor needs to conduct a number of searches to ensure no one else owns the land or property so you can rightfully purchase and own it.

The first step is the finances

Sure, you'd much rather be browsing open homes or daydreaming about decorating your dream home, but your first priority should be getting your finances in place.

Begin with your budget

If you've decided to buy a home, you should have started saving for a deposit, which means you should have a budget in place. Look at your budget and ask yourself how much money can you put towards paying off a mortgage? Where do you spend your money most? And what areas could you start to make savings? Remember to be realistic in your estimations. Consider things such as personal loans, or any planned lifestyle changes like having a baby, and how this will affect your living costs. Be realistic in your estimations; remember you'll need a holiday or two over the next five years!

Work out how much you can borrow

To get an idea of how much you can borrow use a Borrowing Calculator. This will give you an indication of your borrowing power. Keep in mind that repayments typically do not exceed 30% of your pre tax income.

Next look at how long you need to borrow the money for. Longer-term loans with lower monthly repayments may seem appealing, but your total repayment will be higher as the interest stacks up.

Don't just pay the minimum amount. Remember if you only make the minimum monthly repayments; it will take much longer to pay off the balance and cost you far more in the long run.

Remember to work out the interest. Depending on whether you choose a Fixed or Variable home loan rate your repayments may increase or decrease as interest rates change.

You should also take into account any additional fees. There are a number of fees associated with buying your new home. Don't forget to budget for these initial costs when determining how much you need to borrow. At this stage you should also find out whether you are eligible for any government assistance or the First Home Owners Grant.

Work out your deposit

Aim for a minimum of between 5-20% deposit for your home. You may also want to save an additional 5% to cover the settlement costs. Work out if you need to save a higher deposit to avoid Lender's Mortgage Insurance, which normally applies when you borrow over 80% of the purchase price.

What to do if you have a small deposit?

Having a small deposit doesn't mean you can't start your home buying journey, it just means there are a few key factors you need to consider.

Many lenders accept guarantees from family members in support of a loan application. This can reduce or eliminate the cost of lender's mortgage insurance and/or increase the amount you can borrow.

Apart from acting as a guarantor, family members can also assist homebuyers with a low deposit by gifting at least part of the deposit to their children or providing a supplementary interest free loan in addition to the bank loan.

Just remember that while there are ways around having a small deposit, with a larger deposit you will either be able to afford to purchase a better home or alternatively have a smaller loan with lower repayments.

Family Pledge

If you don’t have the option to provide a large-enough deposit on your own, a Family Pledge loan can help you buy a home anyway.

If you have an immediate family member who has a good equity stake in their property, then you can ask them to act as a guarantor for your loan. This may give you the ability to borrow up to the full value of your desired property.

In order to make use of the Family Pledge loan, you still need to be able to make repayments towards the loan on an ongoing basis but the initial requirements for a deposit won’t apply. Once you have paid off enough of the loan and your equity in the home is substantial enough, you can then look at refinancing the loan to pay off your relative.

Fees to be aware of

Keep in mind that there are a number of fees associated with purchasing a property and obtaining a mortgage. These fees can vary from nil to $600 depending on the application.

There are government charges including:

- Stamp duty on purchase and on mortgage amount
- Registration of title transfer
- Registration of mortgage

As well as the following fees:

- Lender's Mortgage Insurance
- Loan Application Fee
- Settlement

Getting approval

People are often confused by the difference between pre-approval and conditional approval when applying for their home loan.

Pre-approval simply means a quick check on your serviceability of a loan has been done and it is calculated that you should be able to make mortgage repayments on the amount you have been pre approved for. It is not binding and cannot be used to make an offer on a property.

Often with pre-approval there is little to no consideration for lending policies, guidelines and rules. However, with Mortgage Street, the pre-approval abides by the business policies and rules, our process is systems generated based on our lending policies to give a more accurate idea of the amount you can borrow.

Before proceeding with any property purchase it is important to get a full or unconditional approval. This involves completing a full application form. You will also need to submit a number of other documents including:

- Pay slips
- Sufficient proof of id for each applicant
- Details of all debts or loans to be paid out
- Details of any recurring income (i.e. rental income, pensions etc.)
- Details of your living expenses etc.
- Details of your previous address if less than three years at current address
- Details of your previous employer, if less than two years at current employment.

The lender will then offer you a conditional approval for the specified mortgage amount subject to you finding a property. At this stage you have an idea of what you can afford before you start looking at houses, so you won't waste time looking at the wrong places. You will know how much you can borrow and what your repayments will be.

Now, it's time for the fun part!

“What we were looking at originally is not what we ended up buying. We thought we wanted something very modern, but we ended up buying something we can make our own and I’m very happy about that.”

Finding a property

When you are looking at places try to keep a very open mind. You’ll start to develop an idea of what you like, what you don’t like, and learn more about the areas in which you want to settle.

It’s best to start browsing on the internet to get an idea of what’s out there and what’s in your budget. Sites such as www.domain.com.au and www.realestate.com.au provide thousands of listings where you can search by price, area and your special requirements such as property type (house or unit) number of bedrooms/bathrooms and car spaces. Once you’ve had a good look online start attending open homes.

But it's all so emotional

Based on the experience of many first homebuyers, the best advice we can give you is to try not to get emotionally attached to a place. While it may look fantastic on the surface, you never know the true character of a property until you've had a pest and building report done.

While there is certainly an emotional element to the purchase, you shouldn't make an irrational emotional decision about buying your home. A good way to combat this is by ensuring your finances are in place and ready to go before you start looking. That way from the very beginning you know what is in your range and what you can and can't afford. Having everything ready to go is also an advantage if you need to act quickly to secure the house you love. Though remember to have all the relevant reports and checks done before you rush into anything.

What will your home give you?

This is one of the most important questions you can ask yourself when buying a home. What can it give you? Do you want a sanctuary; something brand new that needs no work done? Something with all the mod cons that you can just come home to after work and relax in? Or do you want an older house that you can add to, renovate and make your own over time?

Will your first home be a stepping-stone or are you planning to stay for the long term? If you're planning a family, will you have enough space or will you outgrow the house quickly?

For some, the only way of buying a home is to rent it out first. This is because of the tax benefits associated with investment properties. Negative gearing creates a cost saving because you can claim a tax deduction for the difference between the rent received and expenses such as interest, rates and maintenance. This may be just the boost you need to get into the home market, especially if you can live with your parents rent-free for a while.

Please note that if you do this you may not be eligible for the FHOG on this property. You need to weight up the pro's and con's as sometimes the benefits outweigh the FHOG. Our lending specialists will be able to help you work this out.

However more often than not, people are pleasantly surprised when they find out how much they can borrow. This is why we can't stress enough the importance of doing your finances first. It will save you so much stress later on in the process.

Crunch time: the buying process

Once you have found a place you love, arrange with the real estate agent to have a walkthrough of the property. Invite your mortgage broker along for a second opinion. If you are happy with the home, make a conditional offer (on your mortgage application being approved) to the agent. Then, negotiate a 10-day cooling off period with the realestate agent, instead of the usual 5 days, to arrange a building inspection, valuation and pest report.

Your conveyancer can organise these forms on your behalf, or provide you with recommended contacts if you wish to organise them yourselves. However, conveyancing is now regulated, subjected to strict compliance parameters and audits.

The next step is to submit your home loan application. Ask your broker to arrange a valuation ASAP. It may take a week to receive a formal home loan approval.

The final step covers the conveyancing process including the contract of sale. For this stage in the process we recommend using a licensed conveyancer. Often people are afraid to engage a lawyer, as they are afraid of the fee. However, conveyancing is now audited and there are a number of regulations. Deciding on a property is both emotional and stressful, so when it comes to the paperwork, you will need someone overseeing the legalities who knows exactly what they are doing. Our advice would be to start looking for a conveyancer when you first start to look for your property.

Once you have signed the contract and loan documents, you are at the settlement stage. This is when you meet with your conveyancer and solicitor at the settlement venue to exchange title documents for cheques. This is also when the stamp duty is paid. Once settlement is completed you can finally collect your keys from the agent! With regards to post settlement, your conveyancer will arrange the payment of the Council, water authority and strata levies (if applicable).

Going once, going twice, sold to the people who know what they are doing:

So you've found your dream home – and it's up for auction. Firstly, don't panic. Auctions can be very intimidating and it's easy to get swept up in the excitement. Here area few tips to help you through the process and help you stand out from the crowd.

The most simple and effective thing you can do is dress to impress, create the perception that you have the money and budget to beat the competition.

Always position yourself towards the back of the auction; this will give you a good view of your competition so that you can see who you are bidding against.

Ask a question at the beginning of the auction to direct attention towards you. Go for a question that might make other bidders hesitate such as, what about the development plans next door? Is the car park on title? Hopefully these questions may unnerve inexperienced bidders.

Ensure you have a pre-auction limit and stick to it. There is no use getting emotional at an auction and overpaying by tens of thousands of dollars resulting in frightening home loan repayments.

Ask the agent how many contract requests and building reports have been commissioned. If it's likely there will be a lot of competition, wait for someone to make a low bid before placing a higher one about $10,000-$20,000 below your estimated reserve price. For example, if the agent is quoting $270,000-plus and someone opens at $250,000, you should increase the bid to $300,000 to show you mean business. This also cuts out the bargain hunters, as even lower bidders can get emotional and increase their bidding levels - which has a snowball effect of increasing everyone else's budget.

Ask the auctioneer “Is the property on the market? Has the reserve been met and are you selling?” If all goes well, the bidding will stall and the auctioneer and agent will go inside for a break. They may try to convince the vendor to lower their reserve price and put the property on the market for an unreserved sale. (Hopefully, they tell the vendor that there are bidders who won’t bid until the property is on the market.)

Remember to call out all your bids with full numbers. For example instead of ‘$1,000’, say $301,000’, so other bidders hear exactly where the bidding stands. Call out all your bids confidently and assertively like you are not going to stop and will continue until you buy the property. Volley bids straight back without hesitation so it looks like you won’t stopuntil the property is yours.

Break down your bids to slow the bidding if required. For example, if the auctioneer asks for $5,000 bids, offer $1,000 or $2,500 bids so that the momentum is slowed. If you know the property you want to buy is being sold at auction, the best thing you can do is attend a few in the lead up simply as an observer so you know what to expect on the day.

The auction process is highly determined by the risk a client is prepared to take as if you have the highest bid when the hammer hits, your offer is then a cash agreement, which means no cooling off or finance clause entitlements.

At an auction, you are also required to pay a deposit on the day (or next business day) of at least 10% of the purchase price. This is another example of why having your finances in order is vital from the beginning. We recommend getting conditional approval prior to going to an auction. Remember this is the step after pre-approval, which involves submitting a full application.

It’s also a good idea to organise a building and pest inspection prior to auction day so you are aware of any structural problems before you purchase the home.

From an emotional perspective, auctions can be very tough as it’s easy to be caught up in the moment. By doing your homework first, you should be able to determine an indication of the maximum offer – though this is ultimately determined by your own risk tolerance and how high you are willing to bid.

Don’t freak out, but you now own a home

Congratulations! You’ve probably just made the biggest decision in your adult life and you are probably mildly freaking out about it – but that’s okay. After such an intense process it’s completely natural to have more questions and even some post purchase reservations about your new home.

At Mortgage Street, we won’t just leave you to deal with all these issues on your own, we offer additional support for the following 12 months of your home buying journey because believe us – your journey is still only just beginning.

Buying a home will make you and your partner feel more successful. You will feel empowered by the security you now have. You’ll notice how the increased responsibility of having a Mortgage and making repayments leads to other successes in your career, in your social life. Sure it’s challenging, but it’s also one of the most exciting times of your life. Though after the initial euphoria – don’t be surprised if a few doubts sneak their way in.

What happened to my dream home?

On the first night in your new home you will stay awake noticing all the negative things you didn't notice before. All of a sudden the reality of the purchase kicks in with a subtle dose of buyers remorse. How didn't you notice the bathroom was so small? Did you really buy a house that has such an old kitchen? This is normal. Your partner is probably lying awake beside you doing exactly the same thing. The fact is it can take 6-12 months for your new place to feel like home.

The first few months are a period of complete readjustment. You might have moved from a small apartment or sharing with your parents to having your very own home with more space than you know what to do with. You will spend your weekend moving furniture around only to move it all back the way it was the weekend after. You will start planning renovations for every room. But slowly, after time, you're incessant rearranging will stop, you will have gained a more realistic idea of any renovations you may want to complete, and one day you'll be sitting on the couch, watching TV, feeling 100% at home at last.

As a way to combat some of this early unease, Mortgage Street helps you by pre-planning and adding an extra $15,000 to $20,000 on your loan to be used for initial renovations when you move in. We understand that you want to make your new home uniquely yours. Many people get frustrated once they have moved in and realise how much more money they need to make the necessary renovations.

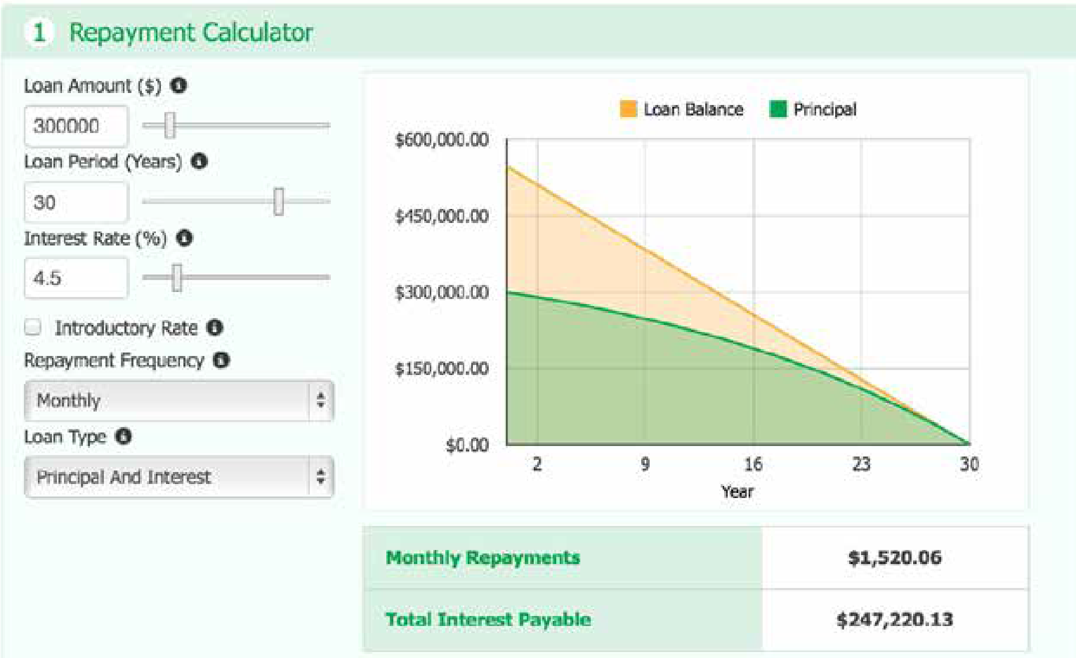
With Mortgage Street, this is no longer a problem, because we will have made sure you considered these costs from the beginning, so you can afford to make the changes you need to feel comfortable in your new home.

While you might be tempted to begin a range of renovations immediately you need to weigh up what is more important – spending $20,000 on renovations now, or paying an extra $20,000 off your mortgage and saving thousands down the track. Not budgeting for renovations is a trap people often fall into and the consequences of borrowing more money can be greater than you think. The graphs below demonstrate the potential savings in interest charges you could achieve by putting $20,000 towards your home loan instead of furnishings and post settlement celebrations. For simplicity, stamp duty, insurance premiums and government costs have been excluded from this example.

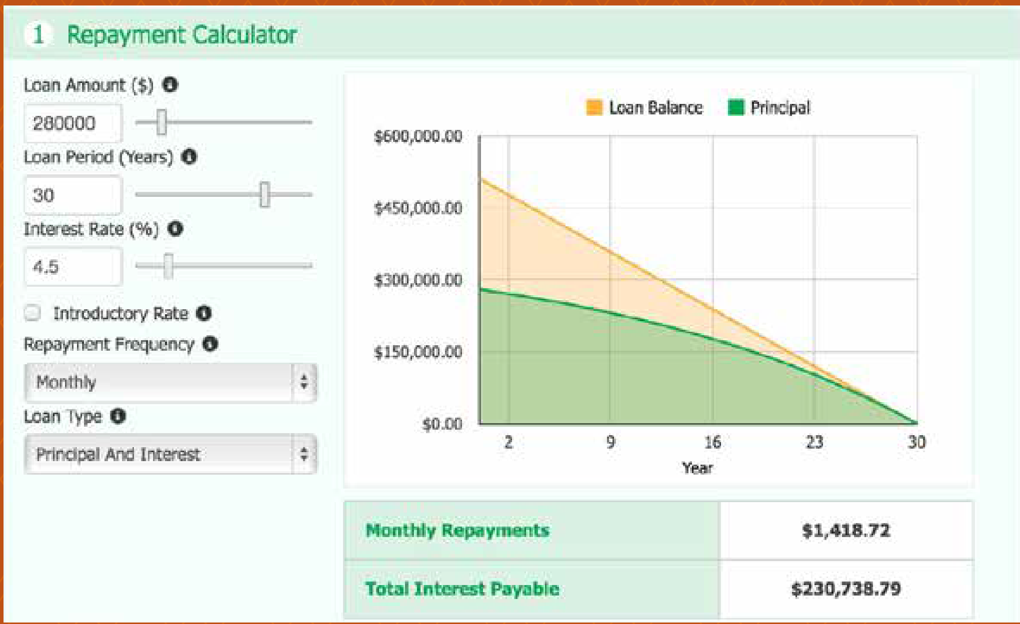
Here's the scenario:

- **You have purchased your own home for $300,000**
- **You have available savings of $20,000**
- **The required loan is either $280,000 or $300,000**
- **Rate applied: 4.5% p.a.**

If you choose to put your savings towards renovations then the results will be as below:



If instead, you decide to allocate your savings of $20,000 towards your home loan, a loan of $280,000 at the rate of 4.5% p.a. would result in the following:



Outcome based on initial deposit:

- Your repayments will drop by $101.34
- You could achieve savings of $16,481.34 in interest charges over a 30 year loan term, allowing you to own your home sooner. In the very first 10 years you would have paid off $16,017.88 off you mortgage.

You should also consider any developments in the area where the property is located that could directly impact the value of your home. This will allow for potential capital growth. For example your property value will increase whilst your home loan balance won't. This opens a range of opportunities, which include raising equity to do those renovations, purchasing your first investment property or taking that holiday!

I thought if I got a home loan, I'd have to give up everything else. I thought my whole lifestyle would have to change cause I was now getting the big "M". But when you run the numbers you realise it's actually so much smarter to buy..

So now i have a Mortgage i can't have a life right? Wrong

It's time to beat the "mortgage myth". Having a mortgage doesn't mean you have to make extreme sacrifices in other aspects of your lifestyle. Yes, you have to be smart about your finances as you have a responsibility to make the repayments, but all of the maths and all of the hard work has already been dealt with. Now you simply have to stick to your pre approved budget.

There is no "trick" to a mortgage. Contrary to popular opinion it isn't designed to disadvantage you in any way. It is designed to take into account repayments that you can afford. If you have just bought a new home you'll have friends going through the same process, don't compare your mortgages. Everyone's financial situation is different.

There is no "right" mortgage. There is only the right mortgage for you.

> *Once you have the house, you have to maintain the house, which is a huge thing!*
> *I mean, we thought about it but we didn't understand it was this whole other ball game.*

Running a home:

If you've been renting or living with family, home maintenance has probably never fallen on your shoulders before. This is the time to admit if you have never actually useda lawn mower...

A lot of people don't realise the ongoing cost of home maintenance and depending on where you've moved to you may not know what local business to use.

12 Months down the track

At this stage you'll probably look back and have a good old laugh about it all. You will have come such a long way, overcome a number of challenges and grown as a person.

But you'll also notice that not everything has changed. You own your own home, but you can still go out to dinner, you can still go to concerts, socialise and enjoy your life. You will have adjusted to the financial changes and your mortgage hasn't become this big weight around your neck dragging you down.

Sure it's a big responsibility, but you might be surprised how empowered you feel. There are loads of emotional and physiological benefits that come with owning your own home. You can enjoy a greater sense of security and a sense that you've invested your money into something that will increase in value over time. You might also find yourself happy to work that little bit harder to own your home faster.

Maybe you've completed a few of your renovations already, maybe you've started landscaping the garden. You will have certainly started creating your own home – and Mortgage Street will have hopefully helped you get your head around it all.

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