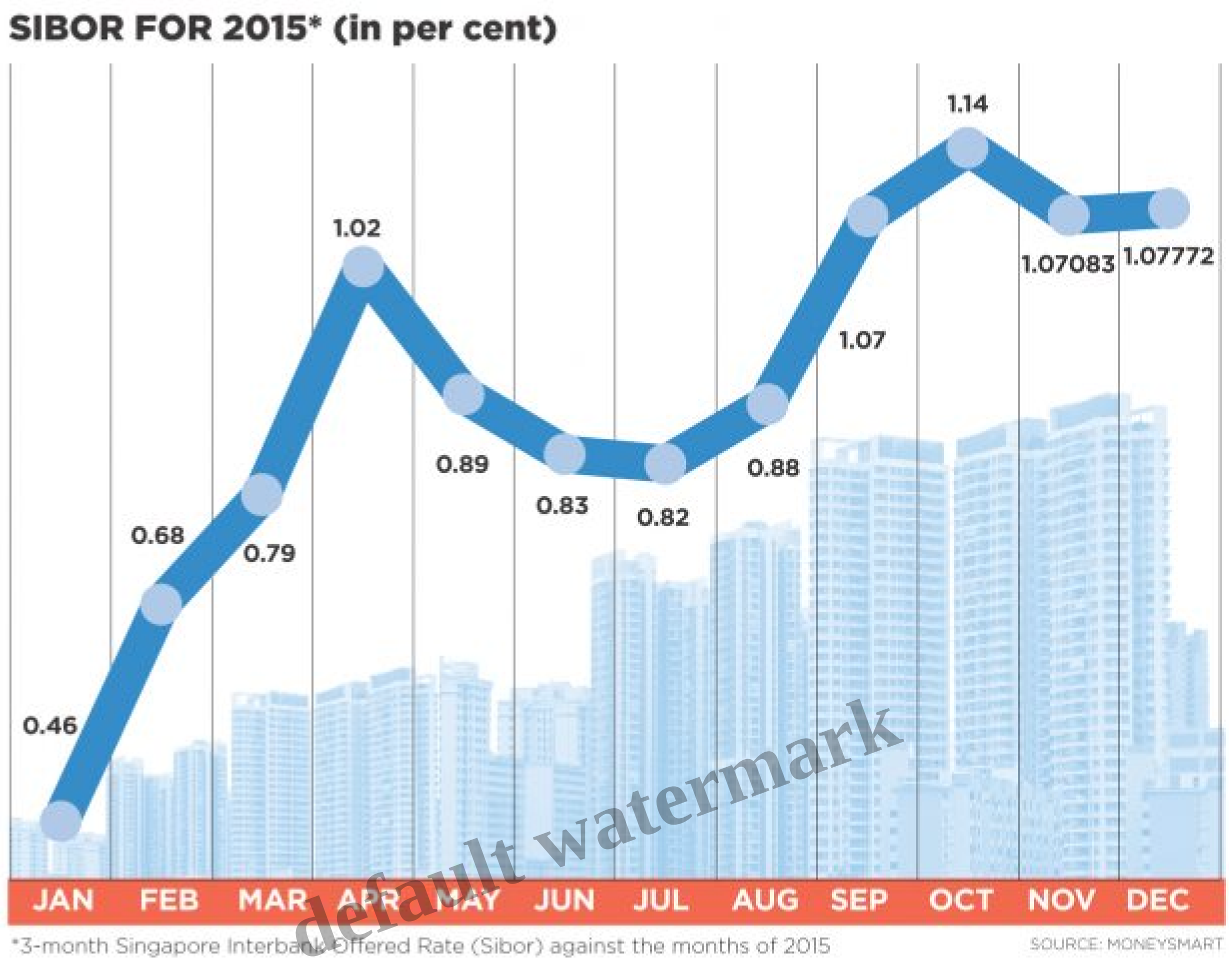
Understanding Home Loans in Singapore

Description

I was chatting with a friend today about how I'm considering investing in REITs, and he reminded me about how the rising interest rates environment are going to impact REITs negatively, since they mostly have high gearing on their properties.
Then I realized, oh dear! REITs won't be the only ones affected when the Fed raises interest rates, because that affects our home loans too!

How Your Home Loan Is Affected by the SIBOR



Source here

Most home loans are pegged to the Singapore Interbank Offered Rate (SIBOR), which is the rate by which our banks lend to each other. The 3-month SIBOR rate is the most often used standard in such floating rate packages, which means the interest rate you pay on your home loan will be revised every 3 months together with the add-on percentage until the next rate review date.

The SIBOR is tied closely to Fed interest rates. The 3-month SIBOR rose to 1.13375%, almost 3 times the 0.44437% level seen just a year ago! This was in December, in the wake of the Fed raising interest rates for the first time since 2006. More Fed rate hikes are expected.

The higher the rates, the more we consumers will end up having to pay on our home loans.
For example, a common loan package we might encounter could be:

3M SIBOR + 0.8% (assuming reduced fees as a sign-up promo).

If the prevailing 3-month SIBOR is 1.1%, then the total interest rate due on your loan for that quarter would be 1.9%.

Source: [CreditFavor]

Are there alternative home loan packages?

On top of SIBOR, you will also encounter SOR (Swap Offer Rate), which tends to be more volatile.

The SIBOR is generally determined by the demand and supply of funds in Singapore between the banks, whereas the SOR is influenced more by external factors such as USD interest and exchange rates. As such, it is also subject to greater fluctuations due to forex movements.

Other than SIBOR and SOR-pegged loans, banks also offer fixed rate packages. DBS also recently became the first bank to introduce home loan rates pegged to fixed deposit rates as another new option. OCBC and UOB has thus followed suit.

As a general rule, floating rate packages are typically lower than fixed rate packages. If you're keen to understand more about home loans in Singapore, I recommend that you refer to this government resource by MoneySENSE here for objective reading.

What should I look out for when choosing a home loan package?

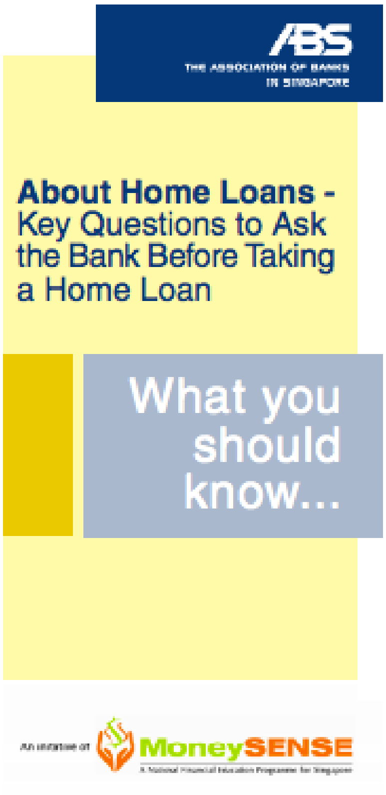
From time to time, banks usually offer attractive promos for home loans. Don't simply look at the headline and the advertised rate though. You should also compare other features such as:

– Effective interest rates (calculate rates for preceding years; I recommend using 3 to 5 years as a gauge).

– Lock-in period. Most banks vary between 2 to 3 years as a minimum commitment, after which you are free to switch to a more competitive offer.

– Cancellation fees.

– Bank subsidies for miscellaneous fees like valuation, legal and conveyancing services, fire insurance, etc.



Check out more questions you should consider in this other online guide here. Ultimately, the most important question you should ask yourself when choosing a home loan package is: **Can I afford the loan instalments?**

Should I refinance my home loan?

Yes, definitely! If you're willing to do a little bit of homework and comparison, switching your home loans can give you quite a bit of savings as the banks compete to win over customers from each other.

Just remember to consider switching costs, like legal and cancellation fees. I wouldn't recommend refinancing before your minimum commitment term on your existing home loan package is up because these fees can add up to more than the savings you stand to enjoy by switching.

Now that I'm due for signing on a home loan anytime (once we find a suitable house, that is), I really hope the interest rates won't be too high when we're ready. Let's hope the interest rates won't rise by TOO much. I'll continue to monitor the situation.

With love,
Budget Babe
Category

1. Property