

Getting ready for rising rates: our Top Tips

It's been a great ride. The past few decades have been an enormous boon to homeowners – who benefited from historically low lending rates and a stellar rise in the values of their homes. Even now, there are no dire predictions of housing market chaos. But when the Bank of Canada told us that rates could rise later in 2010, it seemed like a long way off. The bad news is that this time has come – and we need to get ready for rising rates. How high will rates go? No one has a perfect crystal ball, but we can assume that rates will eventually rise to more normal lending rates of 5 to 6%. Since there is good reason to get ready for rising rates, here are our Top Tips to help homeowners and buyers prepare for what's ahead:

- 1. Don't be tempted to go to the top.** If you are buying a new home, you may not want to borrow your maximum amount. When you're very leveraged, you have fewer options. Interest rates are still so low that homebuyers can be tempted to borrow to the maximum for the best house they can find. It's understandable, but could be unwise in today's rate situation. If mortgage rates rise, that fabulous house could become unmanageably expensive.
- 2. Watch that amortization period.** Many homebuyers are enjoying the lower payments that come with long amortizations. And those 30- and 35-year amortizations can be a great tool, if used wisely. But if you need those long amortizations to squeeze out an affordable monthly payment, you could be in trouble when rates rise and you have no flexibility. To build a buffer, consider taking a 30- or 35-year amortization but have your payments set at a 25-year amortization. You'll be paying more than you are required, which builds that buffer and flexibility that you may need in the future.
- 3. Evaluate the impact of a higher rate on your monthly payments.** If you buy or renew today and lock in for five years, consider what rates could be at renewal and

plan accordingly. For instance, if you currently have a \$250,000 mortgage at 4%, should rates rise by 2.5% in five years, your monthly payment will increase by \$143. If you evaluate the impact of increasing interest rates on your monthly payment today, it may help you to avoid financial difficulties in the future because you can plan accordingly.

- 4. Build some wiggle room into your variable-rate mortgage.** If you have a variable-rate mortgage, you may want to set your payments higher than required, and not use today's ultra-low rate to get an ultra-low payment – so you create a cushion to absorb any rate increases later.
- 5. Pay more.** Another way to speed up your mortgage pay-down is to change from monthly payments to weekly or bi-weekly, and/or by boosting your payment amount, even small amounts can make a big difference over time. Or consider if you can put down a lump sum on your principal, using your tax refund, for example. Lenders offer generous prepayment options so take advantage if you can.
- 6. Watch your other debt too!** If mortgage rates rise, so too will rates on other loans and credit cards. Pay more than the minimum balance on credit cards, and try to have a gap between your credit limit, and what you currently owe. And don't regularly take out new credit accounts.

There's no cause for panic, but there's good reason to be prudent. If you're maxed out on either your mortgage payments or the amount you have borrowed, it could get tense down the road. So now may be the time to get a review of your mortgage situation; take the time to meet with your mortgage planner and scope out the best strategies that will help you prepare for rising rates.

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