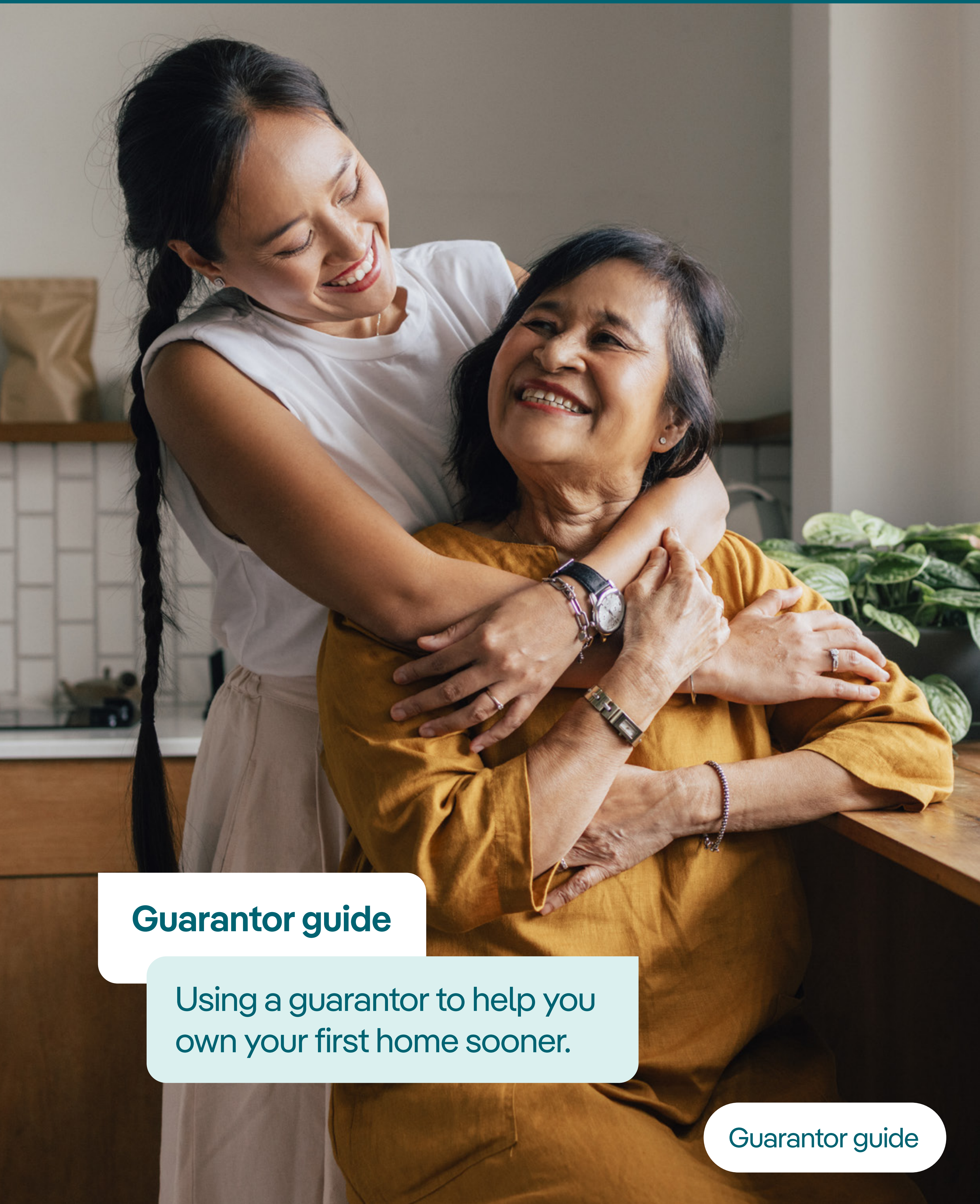
Mortgage Choice



Guarantor guide

Using a guarantor to help you own your first home sooner.

Is a guarantor loan the right option for you?

Buying a home isn't easy

The more property prices increase relative to incomes, the more difficult it becomes for first home buyers to afford a property. Housing affordability in Australia's major capital cities is among the worst in the world based on median house prices and median household incomes.* Some first homeowners save for a decade or more to reach the required deposit for a home loan.

Even if you do have enough deposit to secure a loan, a loan-to-value ratio (LVR) greater than 80% usually means you'll have to pay Lenders Mortgage Insurance (LMI).

So, how can you get a foothold in the property market? One solution may be to use a guarantor loan.

What is a guarantor?

A guarantor on a mortgage is a person who provides the additional security for your home loan if you don't have a sufficient deposit. Most lenders prefer the guarantor to be a close relative – usually a parent, grandparent or sibling.

How does a guarantor loan work?

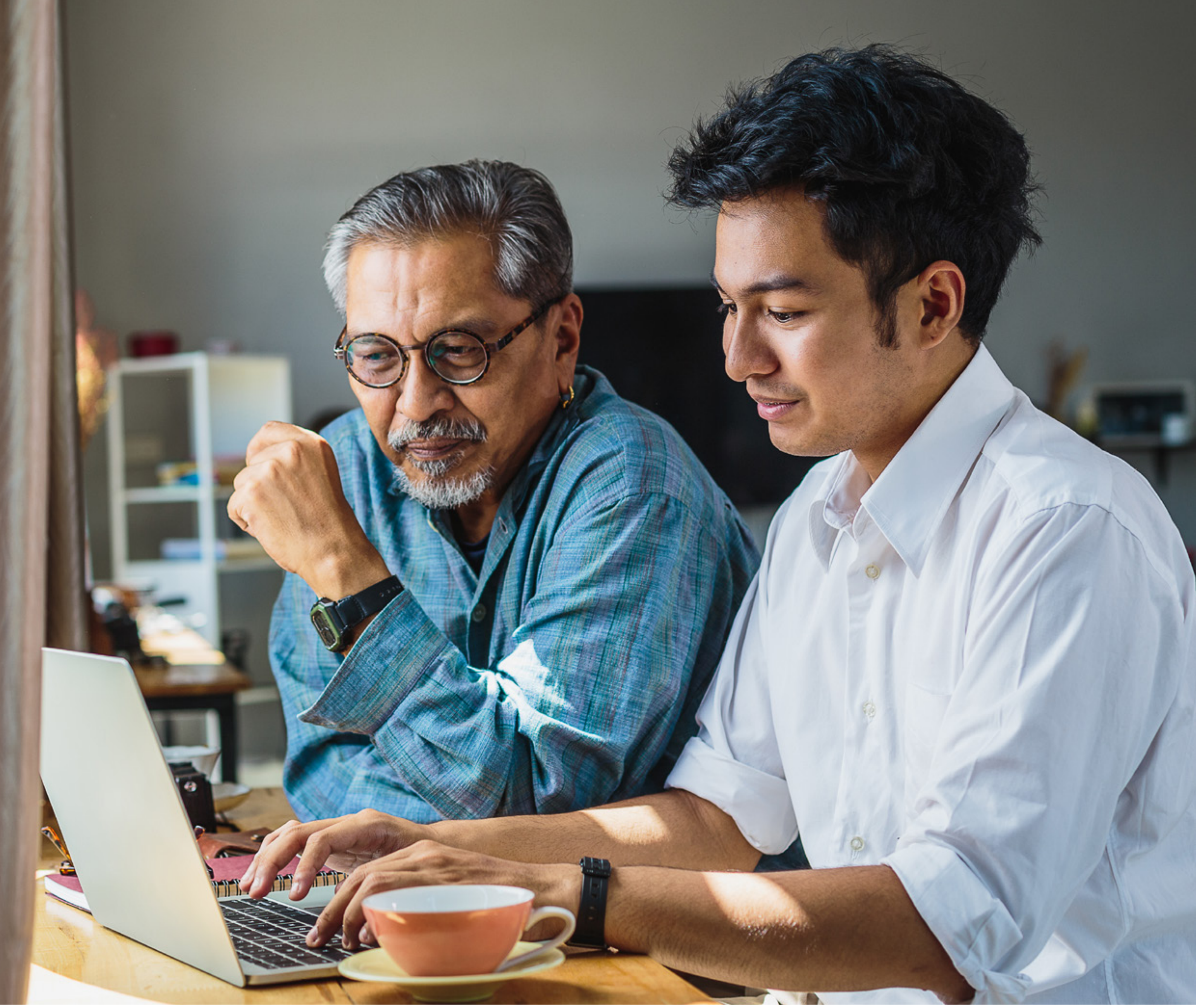
With a guarantor loan, your guarantor can use the equity in their own home or investment property to provide additional security for your loan.

While the primary security for the loan will be the property being financed, the lender will also take a mortgage over your guarantor's property. This mortgage will not support the loan directly but will be used to support the guarantee.

This essentially 'boosts' the size of your deposit, which can allow you to either borrow more money or increase your LVR. The security is usually for only part of the loan amount – usually 20% of your overall loan amount.

Guarantors are different to co-applicants. A co-applicant will be included on the loan and is responsible for the entire loan until it is repaid in full. A guarantor, on the other hand, can be released from the loan once the loan amount reaches 80% of the value of the property.

* How Aussie home price rises compare with the rest of the world, published 13 December 2023 (realestate.com.au)



Example: Using a guarantor

Let's say you would like to buy a $400,000 property. Assuming you have only saved $20,000 (plus purchase costs), you would need to borrow $380,000. You would then have an LVR of 95%, which would incur LMI of about $12,000.

To reduce your LVR to 80% and avoid paying LMI, you would need to save an extra $60,000.

Instead of waiting until you have saved this amount, if a family member owns their own property and is willing to provide a guarantee for your home loan, they can offer $60,000 of their equity as additional security for your loan. This will give you the 20% security you need to avoid paying LMI.

The benefits of guarantor loans

Benefits of using a guarantor loan

- Using a guarantor loan could help you get into the market sooner by reducing the size of the deposit you need to save.
- You may be able to reduce your LVR to an 'acceptable' level, which could be the difference between securing home loan approval or not.
- You could also reduce your LVR to below 80% to avoid paying LMI.

Am I the right candidate for a guarantor loan?

A guarantor loan may not be the right solution for everyone. Your mortgage broker can advise if it's appropriate for your situation. However, in general you:

- Must be able to make the required home loan repayments on the full loan amount by yourself.
- Should have a secure and trusting relationship with the person you're asking to be your guarantor.
- Your guarantor must understand the financial and legal ramifications of the agreement, particularly in the case where you default on your loan.

It's highly recommended that both the guarantor and home buyer seek independent legal and financial advice.

Releasing your guarantor

Your guarantor will be released from their guarantee once the lender can confirm your remaining loan amount is at 80% of the value of your property. This may be when you have paid off the portion of the loan under guarantee, or when there is enough equity in your property for you to take on the loan yourself (if the property appreciates in value), assuming there are no other concerns.

How long this takes will vary depending on the original deposit, the number of extra repayments made (if any) and whether your property has appreciated in value over time.

When releasing a guarantor, you'll usually be required to complete an internal refinance (i.e. with the same lender). In most cases this can't be done automatically, and your lender may need to review your financial situation during the refinancing process.

Depending on the lender, you may have to pay additional fees to release your guarantor. This can include a fee for the lender to revalue your property, as well as lender discharge fees.

Important considerations

For the home buyer

While securing a guarantor may seem like a winning situation for you, it's important to also consider the risks for your guarantor.

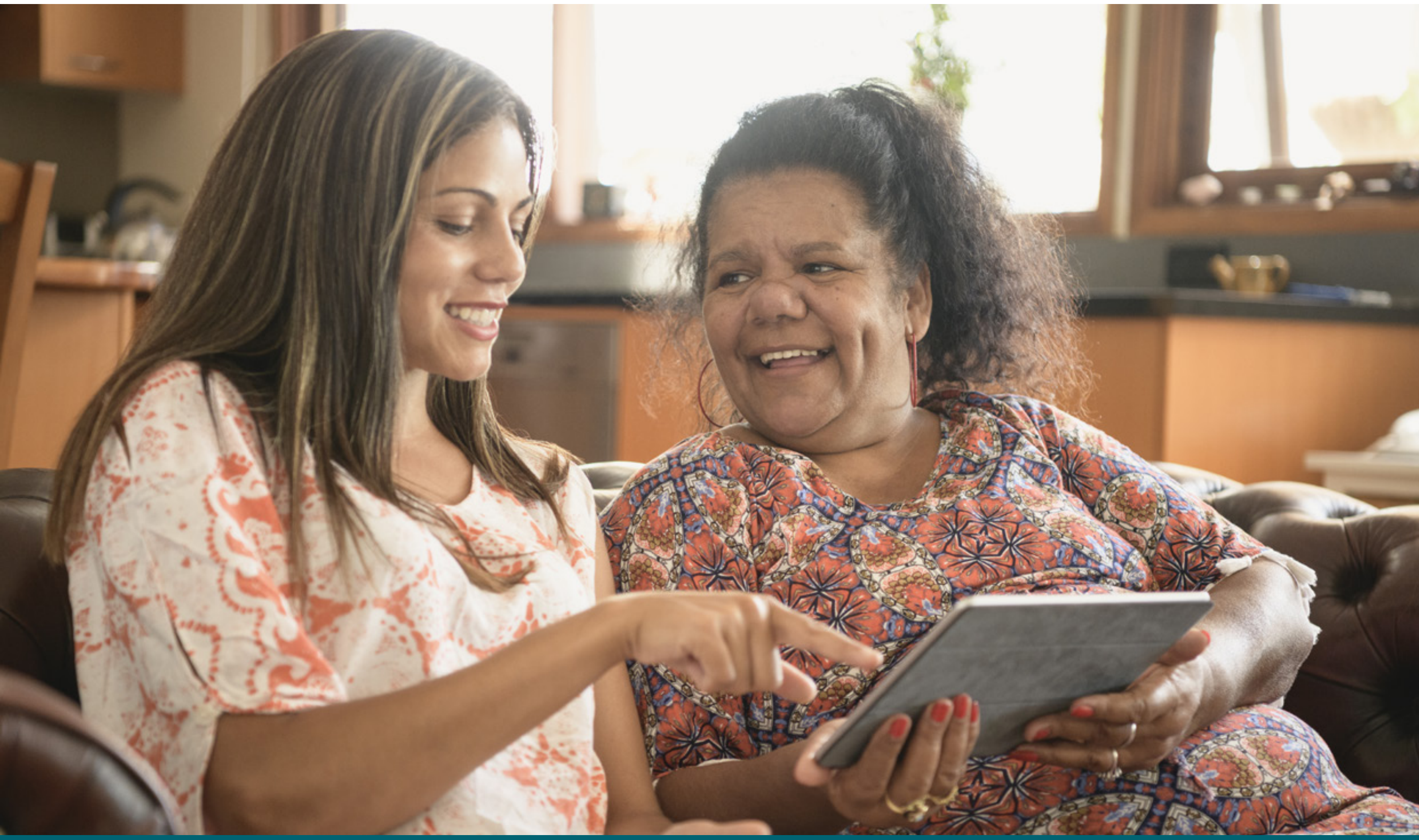
Have an honest discussion with your guarantor about the potential issues, including how they would be affected if you could no longer make your repayments and what you would do if problems arose.

While it may seem like an easy solution to ask a parent or grandparent to act as your guarantor, mixing family and money has the potential to be problematic. Both parties must trust each other completely and guarantors must fully understand their commitment.

For guarantors

It's important to consider how you'd cope financially if the buyer couldn't keep up their repayments, as you could risk having to sell your home to cover the debt. Even if nothing goes wrong, being a guarantor can affect your borrowing capacity. For example, if you wanted to borrow funds to buy a property yourself or renovate your current home, you may not be able to.

Anyone considering being a guarantor for a property loan should seek independent legal and financial advice before accepting the role. In fact, most lenders will insist on this before accepting a guarantee.



A mortgage broker can help you navigate a guarantor loan

While guarantor loans can be a great solution if you are lucky enough to have someone who is willing and able to help you, there are several factors to consider:

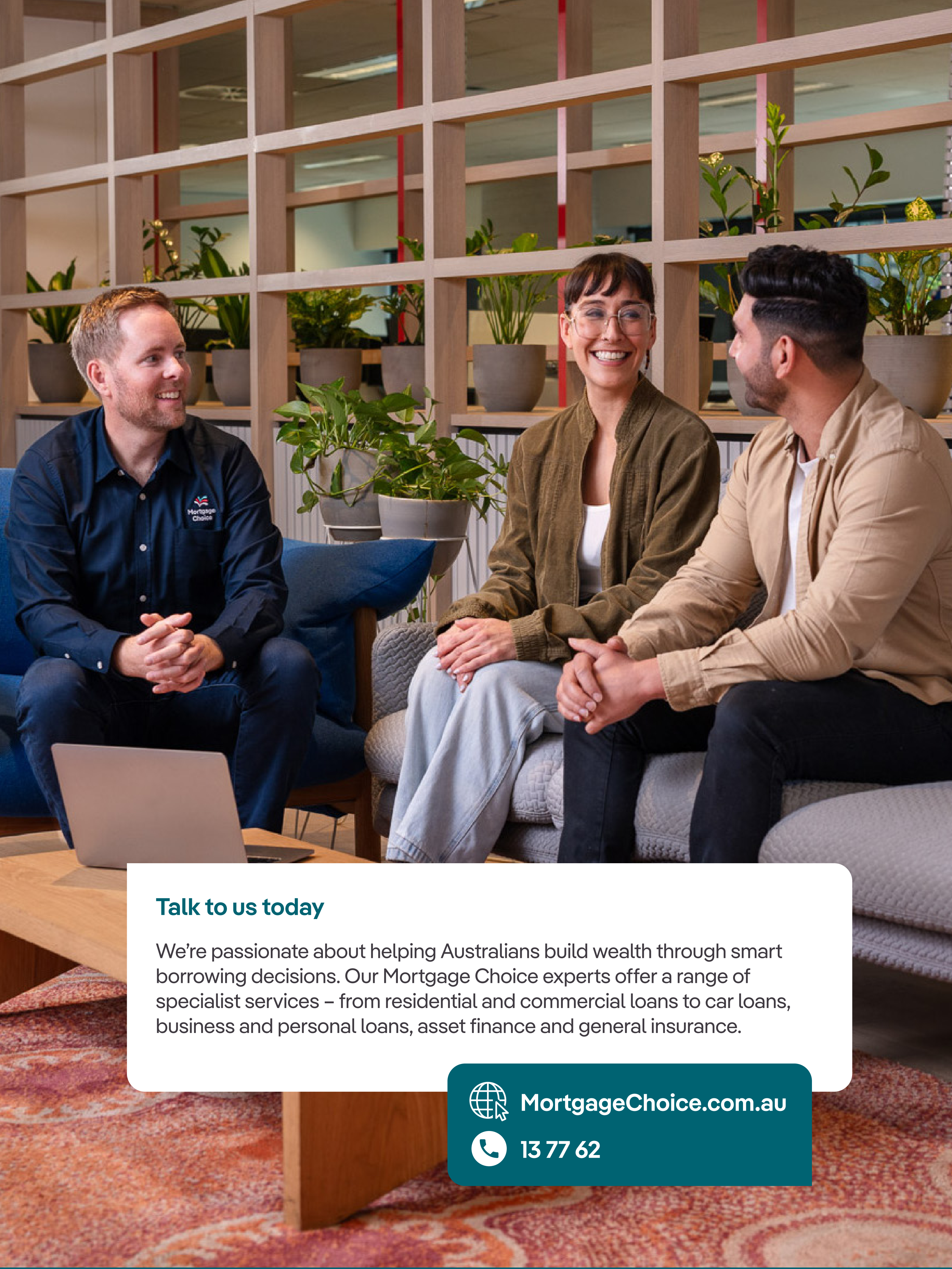
- Is a guarantor loan the right solution for your financial circumstances?
- Is your guarantor suitable?
- Which lender can offer you the most competitive and appropriate guarantor loan?

A broker can explain the different options and help you make informed decisions.

All lenders treat guarantor loans differently. They can vary in the following ways.

- **Who can be your guarantor** – Most lenders will only consider parents and siblings, but others will consider grandparents and other extended family, or even ex-spouses.
- **The amount of guarantee they will allow** – The guarantee can vary from the full loan amount to as little as 20% of the loan (where the loan is for 100% of the purchase price).
- **Fees** – As always, fees vary from lender to lender. You may need to pay some additional fees to release your guarantor. This can include a fee for the lender to revalue the primary security property (the property you are buying) as well as lender discharge fees.
- **The name of the loan** – Some lenders call these loans Family Guarantee Loans or Family Pledge Loans.
- **Release** – Typically, the guarantor cannot be released until you have built up equity in your loan of at least 10% or 20% to avoid paying LMI, but this can vary depending on lender requirements.

A broker can explain the different options and each lender's requirements. They will work to understand your circumstances and find the loan that best suits you and your guarantor.



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