Is it wise to take out a 100% bond while interest rates are low?

By Adrian Goslett

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The recent interest rate cut has stoked the coals in the first-time buyer's market. At least for the next two months until the next interest rate announcement, homeowners are guaranteed lower monthly instalments than in the previous quarter. But, is it wise to take out a 100% bond just to enter the property market while interest rates are low?

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Many first-time buyers want to take advantage of the recent interest rate cut, but do not have enough money saved for a deposit to do so. Our advice to them would be that they seek professional financial advice in order to take a realistic look at their finances and determine if they can afford the implications of a 100% bond.

Banks can justify charging a higher interest rate

For the year ending 31 March 2018, 42.76% of all home loans registered through BetterBond were calculated at 100% of the purchase price. It seems that financial institutions are increasingly willing to grant these sorts of home loans – and it is not difficult to understand why. Banks can justify charging a higher interest rate on 100% bonds because the risk carried by the bank on these bonds is higher than on a bond with a deposit. Buyers who pay a deposit prove their financial stability and lower the total lending amount which therefore increases banks' flexibility when it comes to negotiating a lower interest rate on the bond.

Buyers need to consider the power of compound interest on their home loan. For example, at the end of the 20-year lending period, you will spend just under R50,000 more in interest alone on a R1m bond if you purchase without a deposit. Still, in today's tough economic climate, saving R50,000 over 20 years seems to be a relatively small price to pay when considering how long it might take you to save up for a R100,000 deposit, keeping in mind that you will need to budget for an extra R40,000 or so on top of that amount to pay for transfer duties, bond registration costs and other related fees.

Weigh up the pros and cons

A solution is a sort of marriage between the two options: First-time buyers should consider the option of saving towards a deposit, and then redirecting that money into the monthly repayments on a 100% access bond. This way, buyers do not necessarily need a full 10% of the purchase price saved before they buy. Also, if ever the homeowner runs into financial trouble, or needs the money to do renovations on the home, they can access the money from their bond – an option that would not be as readily available to them if they took out a fixed bond with a deposit.

The truth is that, while it is advisable to have a sizable deposit saved when applying for a home loan, each of the finance options will end up suiting the needs of certain buyers better than others. For example, taking out a 100% bond can help those buyers who want to enter the property market sooner than if they had waited to save for a deposit. Buyers should weigh up the pros and cons of each option carefully and decide which solution works best for their needs.

ABOUT ADRIAN GOSLETT

Adrian Goslett is CEO and regional director of RE/MAX Southern Africa. He joined RE/MAX Southern Africa in 2005 as a franchise development consultant, supporting various regions and offices. Throughout his career at RE/MAX he has held various positions. In 2010, after successfully leading 160 offices and over 1500 agents in six countries through the worst years real estate has ever seen in South Africa in 30 years, Goslett was appointed as CEO of RE/MAX Southern Africa.

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