THE ultimate GUIDE TO mortgage reduction

wealthtoday

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Letter from Wealth Today

Dear Reader

WELCOME TO WEALTH TODAY

Wealth Today was built specifically to facilitate the integration of financial planning into existing appropriate businesses and to provide sound individual financial advice to everyday Australians.

Our mission is to build an accessible, comprehensively supported team of Members who share our vision and commitment to providing tailored financial advice and building a new foundation of financial understanding and security for everyone.

With a national network of like minded experts, we have the potential to provide the financial building blocks for future generations.

KNOWLEDGE GIVES YOU A HUGE ADVANTAGE

We believe that knowledge gives you a huge advantage in creating and effectively managing wealth; in planning to reach your goals; and in being prepared for whatever unexpected twists and turns life may present.

That's why our team of experts has created this series of eBooks that seek to inform you of not only the benefits but also the potential risks and pitfalls of various strategies and investments.

We trust you enjoy this eBook and find it informative and professionally presented. Of course your feedback is always welcome as we strive to continually offer content in a format that is relevant to you.

TAKE THE NEXT STEP

We invite you to meet with one of our authorised representative to discuss what it was you were hoping to achieve when you downloaded this eBook and to establish if they can help you achieve your goals and objectives.

At the rear of this book you will find the details on how to book an appointment with one of our experts.

We look forward to meeting you soon.

Wealth Today

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Introduction

A mortgage is very likely the biggest financial commitment you will ever make. How many times have you heard someone say, 'We don't actually own our home – the bank does!'

If you're one of those people, you've probably thought about how incredible it would be not having to say that any more. To own your home outright is a dream and a goal many of us have. Yet how many of us truly believe it's something that will likely happen in the not-too-distant future?

We're here to tell you that it is possible – and that you can start working toward this goal from today. There are some major success factors which contribute to owning your own home sooner, and what could be better than that? Eliminating bad debt (that debt which isn't providing you with any income or tax benefits) feels good – just ask anyone who's finished paying off a blown-out post-trip credit card bill or car loan!

To anyone paying a mortgage, the idea that you can own your own home is very enticing. It's a huge psychological boost when you do it, providing security and freeing up money so you can do other things.

So how can you really pay off your mortgage faster? Should you re-finance? Will extra features, such as a redraw facility, mortgage offset account or a line of credit be of interest to you? Or should you go for a basic 'no frills' loan instead, and make additional payments whenever you can?

While times have certainly changed, and people are more prepared to use debt to improve their financial situation these days, it is still a dream for many Australians to be able to one day own their own home outright. Unfortunately, the trend seems to be going the opposite way, as today's home loan is not the same home loan as generations past.

Firstly, property values have gone up in proportion to wages, so affordability has decreased. Home loans are therefore larger than they've ever been - in some areas of Sydney, a home loan upwards of $800,000 is normal.

Secondly, a home loan is not just a home loan any more. In reality, it is the total of what you will need to spend on the house to buy, maintain and improve it over several years.

For example, if your house needs a new bathroom in a few years' time, where will you get the funds? If you're like most people, you don't have an extra $40,000 stashed away ready for the next renovation, so you'll likely draw it out of the equity you build up in your house using your redraw facility. Or how about a second storey as your family grows? Again, you won't necessarily have access to the funds at the time you require them, so you'll tack the bill onto your home loan.

There's no doubt about it, the home loan is changing, thanks to a number of factors like our increasing appetite for material goods and the low housing affordability level today.

If you have a mortgage, it is more important than ever to put effort and time into ensuring that you're doing what you can to reduce this non-income producing debt. Avoiding a situation where your home loan needs to be extended (potentially until retirement) should be your priority.

The Three Kinds of Debt

Understanding the different types of debt can help you understand why it pays to reduce your mortgage.

Bad debt is borrowing simply to spend, either on day-to-day things like clothes, or on things that lose value from the day you buy them, like cars and washing machines. This is the typical credit card, car or home appliance finance debt, and it is the worst kind of borrowing.

Good debt on the other hand can fuel personal wealth creation. It's when you borrow to buy an appreciating asset such as investment property real estate or shares. Not only is the asset you buy likely to increase in value over time, but the interest you pay on the loan is tax deductible. So, depending on your income and your tax bracket, you could end up borrowing for your investment virtually tax-free.

Your own home debt has characteristics of both bad and good debt, so it falls somewhere in the middle. Just like an investment property, the value of your residential home should increase over the long term, so that's good. However, you can't claim a tax deduction on the interest you pay on your residential home loan, like you can with an investment property. This is a great pity, because over the lifetime of the mortgage, you will probably pay more than twice the value of the original loan in interest. That is why you should pay your mortgage off as soon as possible. You need to reduce your non-tax deductible total interest bill as much as you can on your residential home loan.

Backyard Treasures

In the popular fable, *The Alchemist* by Paul Coelho, Santiago the Andalusian shepherd boy follows his dream and sets off on a journey. In search of a hidden treasure, he wanders off to faraway places and into the desert. After years and years of endless searching far and beyond, scouring foreign lands, living with Bedouins and Arabians, Santiago finally returns home only to find the elusive treasure he was looking for is in his own backyard.

So, what on earth does this have to do with mortgage reduction, you're thinking? Just as Santiago was looking in faraway places for the answer, you too may be looking outside of yourself for the hidden treasure. You've got the dream home, and maybe even an investment property, and you're now hoping for the magic pill that's going to miraculously wipe out your mortgage overnight.

We've got news for you: the answer is inside of you. There are some fundamental tools you can use to help you on your journey, which we will reveal later, but ultimately, it's your resolve which determines your success. Paying off a mortgage requires sacrifice and discipline, and both these elements must come from within you.

'Tricks' of the trade (like re-paying a loan fortnightly rather than monthly) will help you slash years off your mortgage. We'll explain how this works later in this eBook, tricks like that are not enough on their own. Mortgage reduction is like many things in life: you must be prepared to make the sacrifices required for success.

Many of us don't know the true meaning of sacrifice because our lives have been so plentiful. We've grown accustomed to getting whatever we want, whenever we want it. These more affluent times are a huge contrast to more than 50 years or more ago, when generations of Australians lived through times where basic needs were not something to be taken for granted.

Our standard of living has improved, and creature comforts have become more accessible. At the same time, so has easy access to an endless number of consumer goods, along with credit facilities to purchase them today, whether we can afford them or not.

Having grown up with many luxuries readily available, we've changed our whole perspective of 'want' and 'need'. For example, many kids growing up today will struggle to imagine Foxtel being anything but a bare necessity, whereas 40 years ago, just having a television was a luxury. In many respects, luxury has become the norm. The latest mobile phone, a new iPod, a new car – many of us spend our time accumulating all these things on a regular basis. We've also become used to outsourcing many domestic tasks, such as cleaning, mowing and ironing.

So, what's wrong with all of this? Nothing, if you can afford it. But let's face it, if you were debt-free, had money invested for your future security, with spare cash to spend on the latest model BMW 3 series, then you probably wouldn't be reading this book. Which means it's time you faced the fact that reducing your mortgage is a very worthwhile goal, but one that will probably require you to change your ways on some level to achieve it.

Making larger or more regular repayments on your loan is one of the best ways to reduce your mortgage. That's a simple fact. In the early years of a loan, most of your repayments only cover the interest on your loan. Only a very small proportion of your repayments reduces the principal that you owe. But any extra repayments you can make above your minimum repayment come directly off the principal.

Those spare funds will need to come from money that you would otherwise spend on non-essentials. Quantifying how much time and money those extra repayments can save you on your home loan over the long term will give you the incentive to move forward, so we're going to show you how even your pocket change can transform into thousands of dollars in home loan savings.

Turning loose change into thousands

Making sacrifices is easier when you know the extent of your reward. When it comes to reducing a mortgage, a bit of self-reflection can go a long way. For example, just how much do you 'need' that daily cup of coffee? Or that nightly dose of Foxtel? Or that fancy dinner out each week?

Think of the cup of coffee you have each day on your way to work.

That daily coffee probably works out to $20 per week, or about $86[1] per month. If you were to put that amount into a $500,000 mortgage on top of your regular payments each month instead, you'd save $37,158 and take 2 years off your loan!

Effects of Extra Payment of $86 per month on a Home Loan[2][3]

NO EXTRA PAYMENTS		EXTRA PAYMENT OF $86 P/M	
Loan Amount	$500,000	**Loan Amount**	$500,000
Monthly repayment	$2,684	**Monthly repayment**	$2,770
Total Interest Paid	$466,278	**Total Interest Paid**	$429,120
		Total Interest saved	$37,158
		Time Saved	2 years

You may not decide to kick your coffee habit, but at the very least, this exercise might help you savour that daily cup of coffee one bit more!

The real value of this exercise is that it shows what seemingly small amounts of excess money can do when they are fed into your mortgage on a regular basis. It demonstrates the power of compounding, so the sooner you begin to channel any additional funds into your mortgage, the larger the rewards will be.

Paying off a mortgage is at least a 20-year journey in most cases (although it doesn't have to be), so depriving yourself of things which you cherish is not the answer. It's important to understand though that small sacrifices can be powerful over the long term, and with that in mind, dig deep inside and think about what sort of lasting changes you think you can make to your spending patterns.

[1] $20 per week multiplied by 52 weeks divided by 12 months = $65 per month.

[2] Interest rate of 5% with a term of 30 years.

[3] https://www.yourmortgage.com.au/calculators/

Price versus cost

A helpful tool for helping us reconsider our habits and curb unnecessary spending is looking at the real cost of goods and services. The price of a burger might be $7, but if you're paying a marginal tax rate of 37% like many full-time Australian workers with mortgages are, you need to earn $11.11 before tax to pay for it. Viewing consumables from this perspective can help you consider what they are *really* worth to you, and how much you really want them.

Sacrifice is the act of giving up something you value for the sake of something else more important or worthy. Essentially, it is a deferral of consumption; not spending now, spending later.

You've identified what you want: to pay off your mortgage in the shortest time possible. The first step you need to take is to accept the idea of sacrifice. Only once you've overcome this psychological hurdle will you be able to succeed in reducing your debt.

There's nothing magic about the 'magic pill' we are about to prescribe. It involves making the sacrifices today for better prosperity tomorrow. When combined with having a structure in place to maximise the features available in today's lending products, you'll be on the right track.

Think about what you really need in life Examine what's important to you. What can you live without? If your passion in life is your prized wine collection, doing away with your wine club membership is probably going to leave you feeling deprived. But if your membership is just another thing you have 'because everybody else has it,' or because you're too lazy to change your ways, think again.

Or if you're fairly content with your house, but are constantly pouring money into it because that's what your neighbours are doing, then maybe it's time to re-visit what's important to you.

Or if you're always on the go, eating three meals a day on the run, then maybe a bit of forward planning could make a dent in your expenditure.

No one aspires to be a pedantic number cruncher who whips out the calculator at dinners out with friends, but finding out the cause of 'leaky wallet syndrome' is a necessary evil if you want to get serious about your mortgage reduction. The importance of budgeting

It's important to budget. This is a simple and basic way to help you manage your money effectively, but it's often overlooked. Think of it like a regular dental check-up. Like budgeting, that's probably not something you'd choose to do for fun, but if you don't do it regularly, you can prevent a lot of future pain. If you haven't sat down to do a budget recently to figure out where your funds are going, you're missing a huge opportunity to stop those leaks before they get out of control and prevent you from moving ahead.

There are many budgeting tools available online which are fast and easy-to-use. If you're planning on seeing a financial adviser, they will also help you with budgeting.

The first step on your journey toward reducing your mortgage is to work out what you're willing to sacrifice to be debt-free. Can you differentiate between what you need and what you want? If that line has become increasingly blurred, you may have to do some soul searching to determine whether some lifestyle changes are in order.

My needs versus wants inventory

The Right Stuff

If you have decided that you are willing to make sacrifices towards your goal of reducing your mortgage, you are one step closer to reaching your objective. But the whether this materialises into something that makes a difference comes down to your self-discipline. Self-discipline is about action, or inaction (which is an act itself). All our actions form habits, which lead to consequences, which we may (or may not) like. There are bad habits, and there are good habits. The difference is that good habits help us to achieve our goals.

Some of us are better at self-discipline than others, just as some of us are more prudent consumers than others, and are more aware of how we can be swayed by external factors. There's no doubt that it's not easy to be disciplined with the amount of advertising we are all exposed to these days, and it would be naive to assume that it has no effect on us. Today's marketers are doing their job well. They've had decades of practice and their marketing is often effective. This means your vision needs to be strong and clear, because if you don't have a clear vision, and the resolve which stems from that, you are at the mercy of the barrage of products available.

Are your habits helping you create the vision you're after? Remember, whether you like it or not, your actions are going to achieve an outcome, so make sure it's the one you want. We may be only human, but we do have free will, and the ability to change our behaviour.

Popular personal development blogger Steve Pavlina has a 30-day challenge to help people change their unhelpful habits. Here are the questions he uses in the challenge:

- What new habit(s) can I commit to maintaining for the next 30 days?
- What will this do for me if I succeed?
- When will I begin this 30-day challenge?
- How will I reward myself after 30 days of success?

It can be way too hard to rely on our self-discipline skills on a day-to-day basis if we don't have the right structures in place. Today's consumer-centric world relies on our inability to be disciplined, so we need to make a concerted effort to follow the right path towards our goals.

Creating the structure for success

If you've ever visited the giant online bookseller amazon.com and noticed their 'one-click' shopping feature, you will have seen how easy it's become to spend money. Thanks to technology, we can now buy goods and services anytime and anywhere. If you're looking to cut expenditure, the marketers are doing what they can to make it as difficult for us as possible, but it's ultimately our responsibility to be self-disciplined.

The structure which you surround yourself with – meaning the structure in which your money flows and how you give yourself access to your money – is a make or break element in the mortgage reduction game.

If you already know that you struggle with self-discipline, the best thing you can do is to acknowledge this weakness and put a strategy in place to overcome it. Creating the right structures can force self-discipline.

Putting your finances on autopilot is one part of the equation, but on a more strategic level, you must structure your finances to make sure they are optimised for helping you succeed in reaching your mortgage reduction goals.

Let's say you earn $5,000 a month, and each month you spend $4,990, so the crumb that's left behind is ten dollars. What happens with that stray ten dollars?

You probably wouldn't bother to put it into your mortgage if you had to manually remember to do it. In other words, the easiest thing to do is to leave it in your account.

But what if you put a system in place to capture those excess dollars each month and transfer them automatically into your mortgage?

Having the right structure in place can mean the difference between success and failure. **The most effective way to reduce your mortgage is to make extra repayments, more frequently,** so a structure which lends itself to doing this automatically is going to help you succeed.

Tricks of the Trade

We've talked about the major strategic concepts of mortgage reduction. In this section we will talk about more tactical ideas for reducing your mortgage.

Set your loan up right

Option 1

A structure where your salary goes straight into your mortgage account. This reduces the overall interest you pay on your mortgage debt. You then pay your general expenses by using credit cards – taking advantage of a 55-day interest-free period.

Make sure you're self-disciplined enough to pay off the full balance of your credit card each month, otherwise you won't receive the full benefit of this strategy. You might even get yourself into a debt hole if you don't, because credit cards charge notoriously high interest rates.

To avoid this problem, you should be able to arrange for the automatic payment of your outstanding credit card balance each month.

Option 2

A structure where your mortgage, savings and current accounts are in separate pots. Your savings are used to reduce - or 'offset' - your mortgage. This is called an offset account. The interest you'll be charged on your mortgage will be reduced by the amount that you have in your savings account.

The way your debt is structured can affect your entire financial picture. Some mortgage brokers will be able to provide strategic advice for debt management. Otherwise, find a financial adviser who can help you with your overall planning and cash flow management.

In terms of cash flow management, our financial advisers use a cash hub where all income enters. This provides you with one central operation account for all your cash flows. You can then decide how much to set aside for day-to-day expenses, how much for less frequent, larger expenses and how much for investments.

In this operating account, if there's any excess, it can go back into your mortgage.

Whether you use this type of system or not, it's important to realise that the way you structure your finances can impact the amount and speed with which you pay down your mortgage.

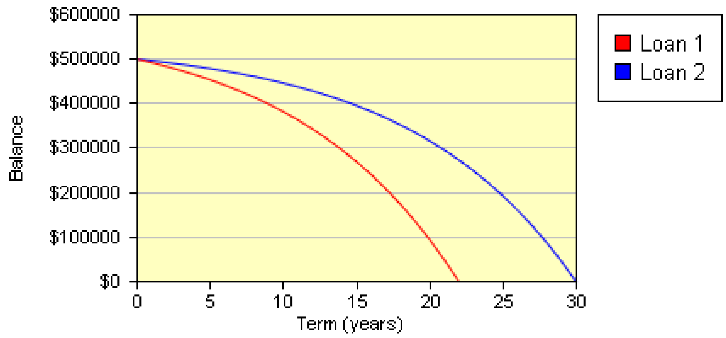
Fortnightly versus monthly repayments

It may seem like magic, but this 'trick' made famous by 1980s money guru Noel Whittaker is simply a way of making an extra payment per year, without feeling the pain.

For example, if your monthly payment on your $500,000 home loan is $2,684 and you arrange to pay half that amount (i.e. 1,342) each fortnight instead, it will feel pretty much the same. That's because there are two fortnights in each month, plus an extra few days.

But those extra few days each month add up over the course of a year, without you really noticing it. Paying fortnightly, you'll make your $1,342 repayment 26 times a year. That's a total of $34,892. However, if you pay monthly, your total repayments would only be $32,208 (12 x $2,684).

So, by paying fortnightly, you really make an extra month's worth of payments ($2,684).



That can significantly reduce both the time it takes for you to repay your home loan, and the amount of interest you'll pay overall.

Effects of Fortnightly Repayments versus Monthly Repayments on a $500,000 Loan[4]

	LOAN 1	LOAN 2
Repayment frequency	**Monthly**	**Fortnightly**
Repayment amount	$2,684	$1,342
Total interest charge	$466,278	$380,459
Total interest saved		$85,819
Time saved		4.75 Years

[4] http://www.choicehomeloans.com.au/calculators/what-are-my-fortnightly-repayments

General tips

In addition to the tricks of the trade we've outlined in this eBook, there are also some general tips for paying your mortgage off sooner.

1. Be careful of honeymoon rates when you're first considering your home loan

Many lenders offer low introductory 'honeymoon' interest rates for the first year or two of home loans to tempt you to choose them.

After that period, the rate converts to their standard rate, which may be higher than you could get initially. That higher rate could cost you significantly over the long-term, even if you start out with a lower 'honeymoon rate'.

2. Consolidate all your debts into your home loan

If you have credit card or personal loan debt, you'll be paying a much higher interest rate than you will on that debt than you will for your home loan.

If you can consolidate that debt into your lower interest home loan, and add the repayments that you were making on your credit card and/or personal loans onto your home loan repayment, you'll pay off all your debts quicker and be in a better overall financial position.

3. Pay all your mortgage fees and charges upfront

When you're first taking out your loan, some lenders will allow you to add their charges onto your loan. Some might even encourage you to do this. Avoid it if you possibly can. You're just turning something that you could take care of now into a long-term debt with interest.

Re-financing

Re-financing can be a way to reduce your mortgage if you can re-finance at a lower interest rate. It's important to shop around to find the best deal, but be aware that most lenders advertise two interest rates with their products – the nominal (headline) rate and the comparison rate.

The nominal rate is always lower than the comparison rate, so it always looks attractive on the surface. The comparison rate is higher, but it includes all the associated loan fees and charges. It is really the true cost of the loan.

Under Australian consumer credit legislation, lenders are legally required to provide you with their comparison rate before you enter into a loan agreement.

Make sure you use the comparison rate when evaluating the loan offers of different lenders, not the nominal rate. That way, you're comparing apples with apples.

If you want additional loan features, look for a low interest rate loan that has them. Paying an extra 0.5 per cent interest for a loan to get features that to help you save money on the surface in the short-term (like an offset account) may end up costing you more than you'll save in the long run.

It all depends on your overall financial situation. Sometimes the extra features are necessary to achieve your tax and investment objectives, so these are issues which should be considered as well. Speaking to a financial adviser can help clarify what type of financing would benefit you the most.

Be aware when you're considering refinancing though that you may incur termination fees for exiting your current loan early, and for fixed rate loans these fees can be high. You will also have to pay the lender's legal fees for discharging the mortgage over your property, as well as fees and costs associated with the new loan (application fees, stamp duty on your new mortgage, valuation and legal fees).

If you're thinking of refinancing, you must do a full check of all costs and fees to make sure you would not be better off staying with your existing loan. Speaking to a mortgage broker can help you to clarify whether refinancing is the best option for you.

Whether you choose to refinance or stay with your existing lender – or even renegotiate with them to find a better deal, the same mortgage reduction principles that we've outlined earlier in this eBook still apply. Sacrifice, as early as possible, pays huge dividends. Only a few spare dollars can help you make huge inroads on your mortgage over a long period, if you are willing to form the right habits.

However, if you 'e not willing to make the sacrifices necessary, then no number of tricks and tips are going to help you.

Conclusion

Paying off a mortgage as early as possible is not a short-term exercise, it's a long-term journey that you're trying to shorten. You might be able to motivate yourself to manage your money and your home loan repayments better for a month or two, but if you don't have the self-discipline to make that a long-term habit, then you're probably not going to make a huge impact in reducing your mortgage.

If you want to pay off your mortgage sooner, you must embark on a voyage that will involve some self-reflection and an understanding of the role sacrifice and self-discipline need to play in achieving your goal.

Knowledge is power, so assess your situation and consider a financial adviser to help you with your planning. Most importantly, remember that having a clear vision for the future is the first step towards creating the habits that will help you achieve your goals.

Please take the opportunity to book a meeting with us to discuss your financing needs. Introductory meetings carry no obligation and are free of charge.

Readers Notes

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We look forward to meeting you soon.

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