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Fixed or floating rate?
Interest rates unlikely to rise, say experts

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CALGARY -- With enough mortgage choices out there to make your head spin and fresh signs that interest rates could be dropping, a good place to broach the subject of home financing is the age-old debate of fixed-term versus floating rates.

CREDIT: The Associated Press

The slowdown in the U.S. housing market may result in interest-rate declines in Canada.

While fixed terms appeal to those with tight budgets who prefer knowing exactly what the month-to-month payments are, a good argument can be made to go with a floating- or variable-rate mortgage -- at least for the short term.

Andrew Moor, president and CEO of Invis, one of Canada's biggest mortgage brokerage firms, said his company is currently advising people to go with a variable-rate mortgage and then maybe lock in once rates come down.

Moor said a "strange anomaly" is occurring now where larger-than-normal spreads between fixed-rate mortgages and bond rates -- which compete against each other for investment dollars -- suggest that mortgage rates are likely to drop over the next several weeks.

As a graphic illustration of this, Toronto-based Royal Bank cut its long-term mortgage rates twice in one week in late September.

Added to this is a growing belief that a looming economic slowdown will force the Bank of Canada to keep its key lending rate unchanged at 4.25 per cent for the next few months and potentially even lower it next year.

Earlier in September, the central bank signalled that a quicker-than-expected slowdown in the U.S. housing market could bring about larger economic problems that would require rate decreases on both sides of the border.

"It certainly seems to us that there's very little risk of the variable-rate mortgages going up in cost over the next little while," said Moor.

Invis says that even with seven rate increases over the past year, people who had variable mortgages still fared about as well as those who had locked into a five-year fixed term.

One potential strategy is to get a variable-rate mortgage, but set the payments at or slightly higher than those required for a five-year fixed term. That way, if rates go up, you're more than covered. And if they don't, then you're simply paying the principal down faster.

Most financial institutions also now offer the ability to hedge your bets and split your mortgage into two pieces -- one that you lock in and one that you allow to float.

Before you get a mortgage, it's important to set goals and clearly know your present financial status and cashflow, says Kevin Gebert, a certified financial planner with Partners in Planning, based in Surrey.

Gebert likes fixed-term mortgages because it allows people to fix their costs, set up a budget and set goals throughout the year to make extra payments that will take down the mortgage faster.

"What's really scary is someone doing a variable-rate mortgage, where they're penny pinching and going into debt but all they can afford is that variable rate," he said.

"And then they don't worry about the future."