What to do with interest

Make the most of home loan rate cuts, writes **Anthony Keane**

INTEREST payments have fallen to their lowest level of household income in more than three years.

The latest Reserve Bank of Australia figures show that households are paying just 9.8 per cent of annual disposable income in interest.

Housing debt comprises 8 per cent alone, while both numbers are the lowest since 2009 and will drop further following the RBA's rate cut last week.

Despite the falling interest bill, households are unlikely to start spending extra cash in the short term, most financial experts say.

"People are scared and are paying off their mortgages and credit cards because of the political spin about the state of the economy," financial strategist Theo Marinis says.

He says interest rates are likely to fall again, most likely in August, but does not believe confidence will rebuild until after the election.

"The next government is going to look like economic magicians," Marinis says. "Companies and people have cut back, paid down debt, and are ready to consume again once uncertainty has gone away.

"Don't be sucked in by the rhetoric. Australia is still doing really well and the future is very bright thanks to our proximity to China and India."

MyBudget director Tammy May says while interest rate cuts have reduced minimum mortgage repayments, in many cases the money is disappearing elsewhere.

"With the increased cost of living – utilities and food – much of the money saved is spent regardless," she says.

May says households should use their rate cut savings wisely.

"It's very easy just to spend the extra money so it's really important to review your budget and make the most of your extra cash flow," she says.

"You could increase payments to your highest interest bearing debts to pay them off quicker, but check your loan contract to make sure there are no penalties involved in doing this.

"You could also have the money you are saving from the interest put into an offset account – this could be an emergency account setting yourself up with a buffer in case of an emergency.

"Or if you have been doing it tough you could use some of the savings to reintroduce an activity into your budget that will improve your lifestyle."

CASH IN ON INTEREST SAVINGS

- Divert your spare cash to the highest-interest debt, usually credit or store cards.
- Pay off personal debt on items that depreciate, such as cars and whitegoods.
- Maintain mortgage payments to pay off the loan faster.
- Put your interest savings into an offset account to act as your emergency fund.
- Make sure changes to your budget are flexible because interest rates will inevitably move higher.

Source: MyBudget, Marinis Financial Group

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