A Fixed Rate Loan allows you to lock-in an interest rate over a predetermined term of 1 to 5 years, providing you with the assurance of knowing exactly what your repayments will be during the term selected, irrespective of whether interest rates change. If you are considering a Fixed Rate Loan as part of your financial arrangements, there are some key facts you should be aware of concerning break costs.

What are break costs?

When you enter into a Fixed Rate Loan agreement, you make a commitment to pay interest at a fixed rate, based on a specified loan amount, over an agreed period of time and we will make arrangements to fund your loan with the understanding that certain fixed payments will be made for the entire fixed rate period. When a Fixed Rate Loan agreement is made, HSBC borrows funds at the applicable wholesale market rate. This allows HSBC to lend this money to our customers, at that period in time, for the term of the fixed rate requested. Just as you have an obligation to pay HSBC, we have an obligation to pay the organisations in market who lend us the money, at a fixed rate, that we use to fund your fixed loan.

If, during a fixed interest rate period:
- you make additional repayments above the allowable threshold (currently at $10,000 p.a.); and/or
- you prepay part or all of your loan; or
- you request to vary the rate on your loan and where we have agreed to change your current fixed interest rate to a new fixed interest rate or to a variable interest rate

we will need to break the funding arrangements that we have put in place for your Fixed Rate Loan. This may result in a loss to us if the current wholesale market rate is lower than the original wholesale market rate at the time your original fixed rate loan was taken out. This loss is then passed on to you as a break cost. The wholesale market swap rates change throughout the day but a daily snapshot is published every day in the Australian Financial Review.

How are break costs calculated?

The calculation of HSBC’s break cost is based on a number of different factors, which include:
- the original wholesale market rate on the date of settlement;
- the current wholesale market rate on the date of prepayment or switch;
- the prepayment threshold we allow you to repay per year (currently at $10,000 p.a.);
- any unpaid interest, fees and charges and any default interest you may have;
- the timing, frequency and dollar amount of repayments required under your loan contract;
- the size of the prepayment; and
- the number of days remaining until the end of the fixed rate period.

For example

Let’s assume you took out a 3 year fixed rate interest only loan for $250,000 and the 3 year market wholesale rate at the time was 8% p.a. You made a lump sum payment and utilised the full repayment threshold we allow you to repay each year. When you’re almost at the end of your loan with 1 year left on the fixed loan term, you decide to pay the loan off early. At the time you pay the loan out early, the 1 year wholesale market rate has moved to 5% p.a.

In this instance the break cost calculation is based on a $250,000 repayment with a wholesale market rate difference of 3% p.a. over the remaining fixed rate period of 1 year.

The loss to HSBC would be approximately $7,500 due to the change in market funding between the time you took out the loan and the time you wish to pay it off early. This loss is then calculated to reflect the present day dollar value of the loss and is passed on to you as break cost – approximately $7,100.

HSBC discloses the fact that a break cost will occur if you pay your loan out early, before the agreed term of your loan, in the Home Loan Letter of Offer which forms part of the contract between you and the Bank.

The Letter of offer also provides you with information about how the Bank will calculate the break cost in the instance you decide to pay off your loan early.

You are always provided with an opportunity to consider the letter of offer and all the Home Loan terms and conditions before you agree to borrow from HSBC. We also recommend that you seek independent financial and legal advice prior to entering into an agreement for a Fixed Rate Loan.

We hope this information has assisted you to understand how HSBC calculates and applies break costs to its Fixed Rate Loan facilities. For more information regarding HSBC’s Home and Investment Property Loans you can refer to our website at www.hsbc.com.au and visit our Home Loans page or call us on 1300 308 008.