

## DAWIE'S NOTES

- Dawie Roodt

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### TO FIX, OR NOT TO FIX, THAT IS THE QUESTION.

The SARB reduced the repo rate, or repurchase rate, by an unprecedented 275 basis points (bpts), or nearly three full percentage points, since the beginning of the year to 3.75%; a record low. And further cuts may be possible!

Of course the SARB's actions are supposed to support an economy in distress. And apart from the cuts in the repo, other measures like a relaxation in the liquidity- and capital requirements of banks, a guaranteed loan scheme in collaboration with treasury, and the buying of state debt in the secondary market, were also implemented.

Unfortunately, although these measures will go some way to support some businesses and individuals and therefore the economy, the effect of these measures are likely to be rather small. The reason is simple: now that interest rates have been reduced, do not expect people to rush out and buy new cars and flatscreen TVs, because confidence in the country is at an all-time low!

Even if interest rates are reduced further, it is unlikely to lead to a spurt of borrowing. Additionally, whenever interest rates are reduced, many, especially the elderly that are dependent on interest income, will see their income fall. So, some will win with lower mortgages and other payments, but others will see their income fall. What are your options then regarding this new interest rate environment?

The reasons for low confidence can mostly be ascribed to a destructive government and the wrong economic policies, but that is not the topic of this article. This article is about interest rates and the decisions that businesses and individuals will be confronted with in this new interest rate environment.

With lower rates, those that do have to pay off loans to the bank are undoubtedly better off and certainly many would like to "lock-in" this windfall. That is the reason why many are considering "fixing" the interest rates on their loans, particularly their mortgage loans.

Most mortgage interest rates in South Africa are "flexible", meaning that this rate changes when the SARB changes the repo rate, as has happened recently. But most South African banks will be prepared to fix the rate of their clients' mortgage loans at a certain level. In the current environment of lowish interest rates it may, therefore, make sense for borrowers to consider fixing their mortgage rates.

Typically, when an interest rate is "fixed", it will be for a limited period of one to three years. Additionally, where interest rates are currently adjusted whenever changes are made to the repo rate, a fixed rate will remain unchanged for the duration of this limited period.

But, and here is the catch, when a rate is fixed, it is usually fixed at between 150 to 300 bpts, that is 1.5% to 3%, higher than the current rate a client is paying. That means that short-term interest rates will have to fall by an additional 150 to 300 bpts or more, and rather soon, for a client to break-even should he/she decide to fix his/her rates.

Further interest rate cuts are certainly possible over the next few months, but few economists expect rates to fall by more than another 50 bpts, which makes the fixing of your rates at these levels probably unwise.

The reason you may want to fix your rates is exactly because you expect interest rates to rise soon(ish). But as mentioned above, most economists expect a further fall in the repo over the next few months. Economists are not expecting a rise soon(ish).

Sure, it is possible for rates to start rising next year or so, and it is certainly possible that rates can be, say, 150 bpts higher than it is today, but I doubt that rates will be 300 bpts higher in a year's time. In three years' time the rates can certainly be 300 bpts higher than now. Or even higher than that.

So, the question to fix or not to fix depends on the level and the duration at which you can fix the rates. Given the current uncertainty about the future trends in the repo rate and the fact that your fix has a time limit, if you fix today and it works out for you, consider yourself lucky.

There is one instance where a fix may be considered and that is where a budget is so tight that it is better to fix at a higher rate for a relatively short period. And remember, banks also have economists that work for them and no bank will ever enter into an agreement if it thinks it will not be making money.

It seems to me the answer to the question might be: Don't fix.

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