



YellowBrickRoad

Home Loans

Let's look at some other examples of how to calculate equity, with some general assumptions. Assuming no limitation of income, here is what could be done with and without lenders mortgage insurance:

Without Lenders Mortgage Insurance:

$$\$700,000 \times 80\% \text{ LVR} = \$560,000$$

$$\text{Equity release} = \$560,000 - \$400,000 \text{ (minus any loan exit costs)}$$

$$\text{Equity release} = \$160,000$$

Using the rule of 4, let's see how that works out:

$$\$160,000 \times 4 = \$640,000$$

Funding required:

Purchase Price	= \$640,000
Stamp Duty (NSW)	+ \$24,000 (approx.)
Other costs (lender, legals, etc)	+ \$5,000

Total Funding required	= \$669,000
Less equity release	- \$160,000

Loan required:	= \$509,000
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$$\text{LVR} = \$509,000 / \$640,000 = 79.53\% \text{ Almost perfect!}$$

With Mortgage Insurance (assuming a maximum LVR of 90%)

$$\$700,000 \times 90\% = \$630,000$$

We can assume LMI is either paid monthly (an option through RWF, or it is capitalised onto the loan).

$$\text{Equity release} = \$630,000 - \$400,000 \text{ (minus any loan exit costs)}$$

$$\text{Equity release} = \$230,000$$

The rule of 4 won't necessarily work if an investment property is being leveraged to a 90% LVR. Loan amount caps and other lender restrictions might come into play.

Here is what could work:

Funding required:

Purchase Price	= \$1,200,000
Stamp Duty (NSW)	+ \$50,000 (approx.)
Other costs (lender, legals, etc)	+ \$5,000

Total Funding required	= \$1,255,000
Less equity release	- \$230,000

Loan required:	= \$1,025,000
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$$\text{LVR} = \$1,025,000 / \$1,200,000 = 85.4\%$$

There is a greater risk associated with gearing property at above 80% LVR, as such Lenders Mortgage Insurance would be required on both loans. Naturally there would also be a greater reliance on your income (apart from rental income generated by an investment property) which would need to be taken into account. This example merely illustrates the power of leverage.