Analysts advise choosing type of mortgage wisely: ROSS MAROWITS THE CANADIAN PRESS

Mar 09, 2009, MONTREAL

Bargain basement borrowing costs are prompting many Canadians to opt for fixed mortgages even though variable products continue to be a money-winning option for the foreseeable future, industry observers say.

Canadian Imperial Bank of Commerce's chief economist says variable rate mortgages should produce the greater benefit for the next two to 2.5 years, but be a wash over five years.

"If you're really risk-averse, jump on those fixed-term rates because they're extremely cheap,'' Benjamin Tal said.

"Going variable probably will give you good performance for the next two years or so and beyond that, we might see interest rates rising.''

Inflation could ultimately lead to higher interest rates, but likely not before 2011, he said.

Variable rates remain attractive even though banks last fall eliminated discounts and began charging premiums for those who signed up for them after the Bank of Canada lowered its interest rate.

The central bank went even further last week, cutting its trend-setting overnight rate another a half percentage point to 0.5 per cent. Banks followed by lowering their prime rate to 2.5 per cent.

Homeowners with variable rates, especially those with discounts reaching 90 basis points, should ignore temptations to lock in now, says Vince Gaetano, vice-president of Monstermortgage.ca.

The self-professed fan of variable mortgages said they give customers control, which is important in the current climate.

Gaetano said homeowners should use this window of low rates to pay down their mortgages.

Owners of rental properties, however, should stick to fixed-rate mortgages to balance steady income with stable interest expenses, he added.

Mortgage expert Moshe Milevsky of York University suspects many Canadians will opt for the security of fixed mortgages considering how low rates have dropped.

But he said the decision about what kind of mortgage to take should never be made in isolation of individual circumstances such as the amount of equity, value of the house, debts and risk aversion.

And in markets where real estate prices are falling, seeking a long-term rate may be more important than the type of rate.

"The last thing you want to do is have to renew your mortgage in a year from now and have the bank say: 'Let's assess what that house is really worth,"' he said in an interview.

Studies conducted by Milevsky have shown that variable rates have historically produced greater savings 88 per cent of the time.

"But in today's environment, you'd be hard-pressed to make a case to continue floating,'' he said, advocating a blend between fixed and floating rates.