Quick GUIDES

nook money

The quick guide to lenders mortgage insurance

Lenders Mortgage Insurance – often referred to as LMI for short – is an insurance that lenders take out to protect themselves. Against what? Against the risk of not being able to recover the full loan balance if the borrower is unable to meet loan repayments.

Typically, lenders require you to pay LMI if you need to borrow more than 80% of the value of the property. This is because you represent a higher risk to them as a lender because you have contributed less equity. Let's look at how it works in a little more detail.

The benefits of LMI

In a nutshell, LMI allows you to get a loan when you don't have a substantial deposit (provided you meet the lender's other criteria of course).

What is the cost of LMI?

LMI is a one-off fee. The amount you pay depends on the size of the loan, the size of your deposit and the lender's policy. You can pay for the LMI upfront using your savings or you can add it to the cost of your loan, which is called capitalisation. It is important to note that if you capitalise the LMI, your loan repayments are based on the higher loan amount.

What happens if a borrower defaults and the property is sold?

If a borrower is unable to meet their loan repayments and there is no other resolution, the property may need to be sold to cover any outstanding loan amount. The LMI insurer will pay the lender in accordance with their LMI policy and could then ask the borrower to repay this sum directly to them.

What happens when the loan is refinanced?

LMI is lender specific, which means if you refinance your home loan to a different lender and you borrow more than 80% of the value of the property, you will have to pay LMI again. If you find yourself in this position, it pays to do your research as the extra LMI cost may outweigh the benefits of refinancing to a lower interest rate.

If the equity in your home has increased or you have paid down the principal on your loan, you may not need to borrow more than 80% with the new lender and therefore can avoid paying LMI again.

Is LMI refundable?

If you terminate your loan early, usually within the first two years, LMI may be partially refundable. Each lender will have their own refund arrangements that's you'll need to investigate.

DON'T Forget

LMI does not protect you in the event you are unable to make the repayments on your mortgage. It is designed to protect the lender. You should discuss personal insurance options such as Mortgage Protection Insurance with your broker to cover any unforeseen circumstances.

Case study

Kristy and Matt

Kristy and Matt have found a home they want to buy for $500,000. Typically, they would need a 20% deposit ($100,000) to secure a loan from their lender. By taking out Lenders Mortgage Insurance, their lender is prepared to provide a loan up to 95% of the value of the home.

This means that Kristy and Matt can secure a home loan sooner with a 5% deposit ($25,000) and stop paying rent. Their lender passes on the Lenders Mortgage Insurance premium cost to Kristy and Matt by way of a fee called a “premium”.

The Lenders Mortgage Insurance protects the lender if Kristy and Matt default on their loan repayments – it does not protect Kristy and Matt.

GOT A QUESTION? *Let's chat.*

Got a question? Need some help? The team at Nook is here to help. Go on, get in touch.

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Important information