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THE LAST WORD

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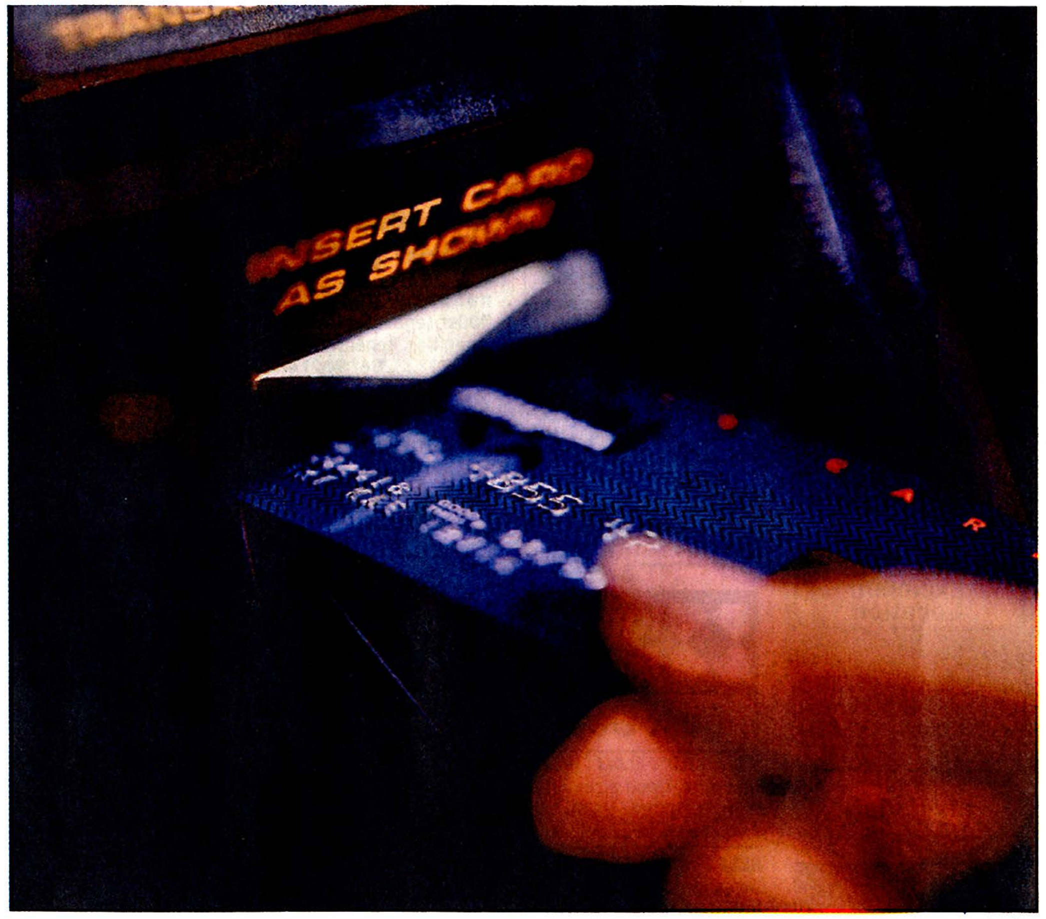
What do bank consumers want?



THIS week, we turn the spotlight on consumers in the competitive world of consumer banking. What are consumers looking for when it comes to the choice of banks?

1. Foreign versus local banks

Foreign banks pay higher fixed deposit rates than our three local banks, yet local banks get the most deposits. Why is this the case? Could the convenience of automated teller machines (ATMs) have anything to do with it?

DBS Bank and POSB have over 1,000 ATMs. OCBC and UOB share a network and together have over 1,000 ATMs.

How about foreign banks? They share a combined network called ATM5, which is made up of seven banks. These are ANZ, Bank of China, Citibank, HSBC, Maybank, Standard Chartered and State Bank of India. Together, they have about 150 ATM machines.

Generally, the ease of access to the ATMs of local banks appeals to more people who want convenience when it comes to making cash withdrawals or other ATM transactions.

But foreign banks offer better deposit rates. For example, DBS offers 0.25 per cent on a 12-month $25,000 fixed deposit. For the same deposit, the Bank of China pays an interest rate of 1.6 per cent.

2. Banks are distributors

Banks have a central role in the distribution of structured products, unit trusts and insurance. They are compensated by charging consumers a one-time distribution fee of 3, 4 or 5 per cent, called a "load".

There are also no-load funds that don't impose this fee, but they are mostly in other countries. We have very few no-load funds here.

Other countries also have many exchange-traded funds (ETFs). They may become "the investment of the future" with their super-low expense ratios. Are we missing out on this trend? One problem is most are US dollar ETFs. Specified investment product (SIP) rules classify US dollar ETFs as risky, partly because they have foreign exchange risk. Trading an SIP is more of a hassle since you need to be "qualified" to trade them, usually by taking a test.

A second reason that ETFs haven't taken off may be that banks won't distribute them. Instead, Singapore banks push unit trusts and ILPs (investment-linked products) on which they earn a commission rather than ETFs where they earn nothing.

A solution might be for funds and ETFs to bypass banks and do their own marketing, which seems to work elsewhere, like in Australia and the US.

Another solution would be to ban commission payments on the sale of all financial products. It sounds radical but here's a surprise: Australia has done it since July 2012 and as the Aussies would say, "It has worked brilliantly". UK has a similar law.

*Quick***Quote**

"It ain't over till it's over."

Baseball great, Yogi Berra, 89, explaining why you shouldn't give up

3. Home loans

Home loans are affordable at the time we buy a home, but we pay off the debt over the years and when the home is half paid for, we may think, "I wish I still had a low 1.5 per cent home loan on the 80 or 90 per cent of the flat's value, like when I first bought it."

Sure, you can always refinance and get close to the interest rate you started with but that is only on the loan's remaining balance. What about the part you have already paid down? Can you renew your home loan on that?

Yes, but not at the original, low interest rate, like 1.5 per cent. You will need to take a personal loan, like a line of credit where rates can be as high as 17.9 per cent.

Why? The collateral is the same. In fact, it is probably better since the property may have appreciated, making it safer for the bank.

"Second mortgages" are standard in other countries, like the US and Europe but they are not as common here. Second mortgage rates are higher than for first mortgages, although the differential is smaller overseas. Will competition usher in a robust second mortgage market in Singapore? We can always hope.

4. Thirty-year mortgages

Getting a fixed-rate home loan is possible. All banks offer them, but there are two points to consider.

One is that fixed-rate loans typically lock in the borrower for three years but lock in the bank for two years. It means banks can raise interest rates after two years and the borrower has no choice but to pay the new interest rates for the third year.

The second point is that here, fixed-rate loans are fixed for a very short time – only two years.

In other countries, like the US, a fixed-rate loan refers to 15 or 30 years. It locks in the bank, which can't change the interest for that period. The borrower, however, is permitted to refinance if interest rates fall.

When banks are locked in for 30 years instead of two, it pushes interest rate risk onto the bank. Here, it is the borrower who must live with the uncertainty of not knowing how much interest they must pay after each two-year interval.

Can our banks consider offering 15 and 30-year fixed rate home loans?

An adjunct professor at SMU, Dr Haverkamp contributes this column weekly to help our readers understand money matters better.