GPL FINANCIAL GROUP PTY LTD
financial planning

Should I put my money into **my mortgage** or **my super**?

With interest rates on the rise and investment returns increasingly volatile, Australians with cash to spare may be wondering how to make the most of it. If you have a mortgage, should you make extra repayments or would you be better off in the long run boosting your super?

The answer is, it depends. Your personal circumstances, interest rates, tax and the investment outlook all need to be taken into consideration.

What to consider

Some of the things you need to weigh up before committing your hard-earned cash include:

Your age and years to retirement

The closer you are to retirement and the smaller your mortgage, the more sense it makes to prioritise super. Younger people with a big mortgage, dependent children, and decades until they can access their super have more incentive to pay down housing debt, perhaps building up investments outside super they can access if necessary.

Your mortgage interest rate

This will depend on whether you have a fixed or variable rate, but both are on the rise. As a guide, the average variable mortgage interest rate is currently around 4.5 per cent so any money directed to your mortgage earns an effective return of 4.5 per cent.[i]

When interest rates were at historic lows, you could earn better returns from super and other investments; but with interest rates rising, the pendulum is swinging back towards repaying the mortgage. The earlier in the term of your loan you make extra repayments, the bigger the savings over the life of the loan. The question then is the amount you can save on your mortgage compared to your potential earnings if you invest in super.

Super fund returns

In the 10 years to 30 June 2022, super funds returned 8.1 per cent a year on average but fell 3.3 per cent in the final 12 months.[ii] In the short-term, financial markets can be volatile but the longer your investment horizon the more time there is to ride out market fluctuations. As your money is locked away until you retire, the combination of time, compound interest and concessional tax rates make super an attractive investment for retirement savings.

Tax

Super is a concessionally taxed retirement savings vehicle, with tax on investment earnings of 15 per cent compared with tax at your marginal rate on investments outside super.

Contributions are taxed at 15 per cent going in, but this is likely to be less than your marginal tax rate if you salary sacrifice into super from your pre-tax income. You may even be able to claim a tax deduction for personal contributions you make up to your annual cap. Once you turn 60 and retire, income from super is generally tax free. By comparison, mortgage interest payments are not tax-deductible.

Personal sense of security

For many people there is an enormous sense of relief and security that comes with having a home fully paid for and being debt-free heading into retirement. As mortgage interest payments are not tax deductible for the family home (as opposed to investment properties), younger borrowers are often encouraged to pay off their mortgage as quickly as possible. But for those close to retirement, it may make sense to put extra savings into super and use their super to repay any outstanding mortgage debt after they retire.

These days, more people are entering retirement with mortgage debt. So whatever your age, your decision will also depend on the size of your outstanding home loan and your super balance. If your mortgage is a major burden, or you have other outstanding debts, then debt repayment is likely a priority.

Older couple nearing retirement[iii]

Tony and Elena, both 60, would like to retire in the next few years. Together they earn $180,000 a year, excluding super, but they still have $100,000 remaining on their mortgage. Tony has a super balance of $600,000 and Elena has $200,000.

They want to be debt free by the time they retire but they are also worried they won't have enough super to afford the lifestyle they look forward to in retirement.

If they do nothing, at a mortgage interest rate of 4.5 per cent it will take five years to repay their mortgage with monthly mortgage payments of $1,864. At age 65, their combined super balance will be a projected $1,019,395.

Jolted into action, they decide they can afford to put an extra $1,000 a month into their mortgage or super.

- If they increase their mortgage payments by $1,000 a month, the loan will be repaid in three years and two months. But their super will only be a projected $931,665 by then, so they may need to work a little longer to fund a comfortable retirement. From age 63, they might consider salary sacrificing into super with money freed up from early repayment of their mortgage.
- If they salary sacrifice $1,000 a month to super from age 60, their combined super balance will grow to a projected $1,082,225 by the time they are 65 and their home is fully paid for.

These are complex decisions, but whichever option they choose they will probably need to consider working until at least age 65 to be debt free and build their super.

All things considered

As you can see, working out how to get the most out of your savings is rarely simple and the calculations will be different for everyone. The best course of action will ultimately depend on your personal and financial goals.

Buying a home and saving for retirement are both long-term financial commitments that require regular review. If you would like to discuss your overall investment strategy, give us a call.

i https://www.finder.com.au/the-average-home-loan-interest-rate

ii https://www.chantwest.com.au/resources/super-members-spared-the-worst-in-a-rough-year-for-markets/

iii All calculations based on the MoneySmart mortgage and retirement planner calculators.

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