

Industry consultant Mehrdad Yousefi says the restrictions imposed on interest-only mortgages by a number of lenders recently are sensible at first glance but they have the potential to affect the house purchase market in some parts of London and the South-East.

"Given that there are still limited funds available for lending and there are not enough lenders operating to stimulate competition many borrowers will find it difficult to secure affordable mortgage deals," he says.

"This is because most will have to find a 25% deposit to get a competitive rate. Moreover, many individuals living in London and South-East will need to borrow between 3 x and 3.5 x income to buy even a modest property in the £180,000 to £270,000 range. If they have to pay on a capital repayment basis in the first two or three years many will not pass lenders' affordability tests."

Yousefi says that in central and greater London, once you look beyond cash buyers and foreign nationals, a consumer would have to earn an above-average salary of £40,000 to afford a mortgage of, say, £120,000 or £135,000 which is 3 x or 3.5 x salary on a repayment basis in the first few years.

So with the virtues of interest-only clear, what could lenders do to help first-time buyers in light of criteria changes that could leave the most needy beyond the reach of the product?

"It's important that customers should have a choice where appropriate, but also that this choice accurately reflects the additional risk of the product," says Stockton.

"Interest-only has been cited as a way of helping first-time buyers because of the reduced monthly pay-

ments but when you factor in the cost of maintaining a repayment vehicle it's not always true to say it's cheaper.

"Like all borrowers, first-time buyers need to regularly review their repayment vehicles and ensure they're on track," he adds. "We're committed to supporting first-timers with products that are appropriate. The changes that we've made to interest-only don't alter that commitment."

And Cliff says Santander too is always looking at ways to help first-time buyers.

"For instance, we have our Homebuyer Solution which offers first-timers and remortgage customers free valuations and £250 cashback to help with costs," he says. "And in recent months we have also increased our maximum LTV on new-build properties, offering 80% LTV for flat buyers and increasing this to 90% LTV for house buyers."

While neither Lloyds group nor Santander cite the credit crunch as the primary reason for changing criteria one wonders whether an improvement in the funding situation might prompt either lender to revise their changes.

"This is the right time to review interest-only, given its increase in popularity among new borrowers," says Stockton. "As with any lender we will always review our policies in line with the market to ensure they are appropriate."

Cliff is equally vague, saying that the lender is comfortable with the measures it has in place for interest-only lending and has no immediate plans to change these.

"We will track developments in the market and review our strategy on an ongoing basis," he adds. "This is not a matter of market conditions or funding, it's a matter of maintaining a prudent and resilient lending strategy."

Given the turbulence the market has experienced it's not surprising that lenders' attitudes to risk have changed. But interest-only mortgages have long offered first-time buyers a chance to purchase a home in an otherwise hopeless situation.

If lenders put these deals beyond the reach of first-timers now it would be in everyone's interests for them to come up with a viable alternative to prevent aspiring home buyers being driven even further from the market. ■

A knee-jerk reaction won't help

“The consequences of any proposals need to be evaluated over a period of time



DALE JANNELS
SALES AND MARKETING DIRECTOR
ALL TYPES OF MORTGAGES

In the 1980s, long before I joined the mortgage sector, interest-only mortgages were often subject to higher interest rates than repayment deals, with the repayment vehicle usually being an endowment policy.

Some 30 years later this interest differential is again being enforced by lenders, leaving repayment mortgages with cheaper rates. Cynics may argue that this is to curb the advance of interest-only.

And the future of interest-only is indeed a big debating point. There are widely differing views on the subject and, depending on individual circumstances, who is to determine which is right or wrong?

Why should either lenders or regulators be able to dictate which is the permitted route for borrowers when everyone's circumstances are different?

All too often, interest-only mortgages have been sold based on ease rather than circumstances. Any sane adviser should ensure that clients have the means to repay the capital debt on or before their retirement date.

But how does this fit with a client who is looking forward to a large lump sum payment on retirement and wishes to enjoy lower outgoings in the meantime? Or one who receives annual bonuses and prefers to have an offset-type interest-only mortgage, using their bonus lump sum to pay into their mortgage when they get it?

And what about those who have been hit hardest in recent times – the self-employed? Many lenders shut the door on this group of borrowers yet they are often the ones who rely most on the flexibility of interest-only to tie in with fluctuations in their incomes. After all, those who manage business budgeting are likely to be the most astute when it comes to managing their own finances and plans for repaying their mortgage.

Repayment mortgages provide the certainty of clearing debt at the end of the term for both lenders and consumers, while lenders are trying to avoid risky lending. And although the Financial Services Authority has demanded tighter controls on interest-only in its Mortgage Market Review, there is a need for it to think outside the box.

The financial impact on first-time buyers in terms of set-up costs and monthly outlay when they purchase a property should be taken into account. For larger loans, the risk involved with interest-only appears to be greater, yet often this type of borrower will be a higher earner with the ability to make capital reductions.

That said, we need a sensible approach to this argument and a rational agreement as to who does or does not suit the profile. There's no right or wrong answer when it comes to interest-only and the consequences of any proposals need to be evaluated over a period of time rather than dashing into a knee-jerk reaction.

● **Too much energy is being wasted worrying about interest-only when some other areas of lending are considerably more risky**