



Buy to Let Mortgages

Introduction

Mortgages can be confusing since there seem to be so many different types of home loans available. This can be particularly true within the buy to let mortgage market, as there are a number of differences from residential mortgages that it is wise to be aware of before you commit to buying a rental property.

Therefore, it makes sense to talk to an Independent Financial Adviser. With the number of mortgage choices available – well over 10,000, constantly changing, different deals from over 100 lenders – we are well placed to help you select the type of mortgage that best suits you. We have access to most, if not all, of the latest mortgages (including many that aren't available through high street lenders), and can provide invaluable assistance in highlighting potential pitfalls.



Repayment or interest only mortgage?



There are two basic ways of paying off a mortgage: repayment and interest-only, with repayment mortgages generally being the preferred choice for residential mortgages. However, for buy to let mortgages interest only is the normal choice and the lender will not expect you to make payments into a separate investment plan.

As the name suggests, with interest only mortgages you simply pay interest to the lender during the course of the loan. Your debt never reduces and at the end of the agreed mortgage term you owe your lender exactly the same sum as at the outset. With a residential mortgage in order to pay off the outstanding capital sum you will normally have to make payments into a separate investment plan, which is designed to build up sufficient funds to repay the debt in full. However, with a buy to let mortgage the rental property is considered to be the investment that will be used to repay the loan at the end of the

term, and hence there is no need to have a separate investment plan running alongside the mortgage.

The benefit of this is that the monthly mortgage payments are lower than for a repayment-type mortgage.

Borrowing Limits

There are two main ways that the amount you are able to borrow through a buy to let mortgage will be limited:

- By Loan to Value (LTV). This is a percentage figure and is calculated by dividing the amount you intend to borrow by the purchase price or value of the property, and then multiplying by 100. For example borrowing £150,000 against a house worth £200,000, gives an LTV of 75%. The majority of buy to let mortgages are limited to a maximum of 75% LTV.
- By rental coverage. This is a way of calculating the margin between the gross rental income and the monthly mortgage payment, to ensure that there is an excess in monthly income to allow for maintenance costs, agents fees, void periods, etc. This calculation varies with each lender but a good rule of thumb is that:

The gross rental income should be at least 125% of the monthly mortgage payments

For example:

If you needed a mortgage of £100,000 to buy a property, the lender would need a rental income of around £625 pm to support this size of mortgage (assuming an interest rate of Base + 0.5%, which gives us a rate of 6% currently).

$£100,000 \times 6\% = £6,000$ annual mortgage cost,
 $£6,000 / 12$ months = £500 per month mortgage payment
 $£500 \times 125\% = £625$ per month rental income

Different types of property or tenants

There are a number of different types of property or tenants that mortgage lenders are less keen to accept when assessing a buy to let mortgage application. The following is just a selection:

- Students
- DSS tenants – where the rental is wholly or partial paid through state benefits
- Houses in Multiple Occupancy – where there are more than one family or household living in the property, e.g. bedsits
- Ex-council or housing association properties, particularly flats
- Holiday lets
- Mixed use, where part of the property is used as commercial premises

This is not an exhaustive list, and there are lenders who will lend on these types of properties or tenants, but often your choice of lender may be limited, which can mean the mortgage deal you are able to secure might not be quite as competitive as otherwise.



The importance of independent financial advice

Buying a property, be it your own home or a rental property, is often a large financial undertaking, and the mortgage required to do this forms an integral part of this investment, so it pays to explore all your options. We are legally obliged to act on your behalf, without bias towards any one particular mortgage provider. We have access to the whole product market, covering all of the latest mortgage deals, as well as exclusive offers that you can't get from bank or building

society branches. In addition, we will be able to highlight and explain any potential pitfalls, such as early redemption penalties and tied-in insurances that can often take the gloss off mortgages that have attractive headline interest rates.

We will consider your overall circumstances to ensure your mortgage works as cost-effectively as possible alongside your other financial arrangements.



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Further Information

For further advice and assistance contact Monahans Financial Services Ltd on **01225 785570** or e-mail us at invest@monahans-fsl.co.uk