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Your Free Guide to First-time Mortgages

Please find enclosed your free copy of the *MoneySavingExpert.com Guide to First-time Mortgages*, sponsored by L&C.

A mortgage to suit

The guide provides a great starting point towards understanding how money can be saved by finding the best possible mortgage to suit you. Just as your requirements are different from the next person, so there are multitude of mortgages on the market. It's important to find the right one to suit your circumstances.

A pleasant surprise

Many of our customers phone us thinking that they will be unable to get a mortgage. Perhaps they have a poor credit history, are a first time buyer struggling to get on the ladder, have an unusual buy-to-let case or have been turned down by another lender or broker. So it is a pleasant surprise when they realise that we can not only help with our expert advice, but that we will not charge a broker fee for our award-winning service.

Another surprise is that mortgage hunting can be surprisingly simple – because we do the work for you. The whole process is conducted quickly over the telephone, with back up and advice provided throughout.

For a no-obligation review, simply call us on: **Freephone 0800 694 0444**. Alternatively, complete the enclosed Freepost enquiry form, return it and we will call you.

We look forward to hearing from you – and finding the very best mortgage to suit your needs.

Yours sincerely,

Phillip Cartwright
Managing Director

Martin Lewis'

MoneySavingExpert.com

THE FIRST-TIME MORTGAGE GUIDE

SPONSORED BY

L & C

Printed May 2010

Independence and integrity

This guide is sponsored by London & Country mortgages, that's the reason it is free. So let us make something very plain. This guide is written with absolute editorial independence. What's in it is purely dependent on our view of the best ways to save money and the sponsor's view on that is irrelevant.

However, the reason we agreed to allow London & Country to be the sponsor, which enables this printed guide to exist, is because after detailed research into those brokers that offer coverage nationwide, London & Country has come out top for each of the last few years.

It's very important that this is understood and no one thinks it is the other way round: that it is being recommended because it sponsors the guide. Like everything with MoneySavingExpert.com, the editorial (what's written) is purely about what's the best deal. If London & Country no longer offers the deals it currently does, and either starts charging fees or stops being whole of market, we'd ditch our recommendation immediately. You can check if that's happened via an up-to-date article on mortgage brokers on the site. Just go to **www.MoneySavingExpert.com/mortgages**

All information correct at time of going to press, May 2010.

Contents

Martin's Mortgage Moments

Written by Martin Lewis, Guy Anker and Jennifer Bailey

Who's this guide for?

It's for anyone who wants to buy a property and needs to persuade a financial institution to lend them the cash to make it happen. The UK mortgage market at times has been one of the most competitive in the world, yet the number of deals available has shrunk since the credit crunch.

There may be a deal out there for you but it's got tougher so the aim is to help you find the best deal, and to help determine whether you're eligible for it. It's specifically for ...

First Time Buyers

Those who don't own a property and are looking to buy one. Whether you can prove your income or not, or whether you've got a good or bad credit history, this guide will explain your options.

Those Considering Property Investment

If you want to buy a 'buy to let' investment property for someone else to live in and need a mortgage for it.

Who this guide isn't for?

Remortgagers

If you already have a mortgage and are looking to move lender, or you simply want to cut the cost of your mortgage, then there's a special guide just for you, go to **www.moneysavingexpert.com/remortgageguide** to get it.

Martin's Mortgage Introduction

Getting a mortgage is one of the biggest financial commitments you're likely to make and thus it should be taken seriously. However, while it's scary, it needn't be difficult. There's a big advantage to getting a mortgage over other financial products.

While I'm normally sceptical of financial advisers and believe you can do better going alone, in the mortgage market, you can get top notch advice without paying anything.

For most people, that's exactly what you should do, so you may ask "why bother writing a guide?" and if you did, it'd be a good question.

The answer is simple: because mortgage brokers are advisors not instructors. Ultimately, it's you who takes the decision and you whom the decision impacts. Even though you're taking advice, understanding exactly how it works is the best weapon possible.

And by the end of this guide I hope you'll not only understand how to get a mortgage, but how to get the best MoneySaving mortgage possible.

1 What type of mortgage to choose

A mortgage is a loan to buy a property, but it has two special characteristics.

- **It takes a long time to repay.**

It's designed to be paid back with interest over a long period, typically 25 years. That means while interest is applied slowly over time, you still pay a lot of it.

- **The loan is 'secured' on your home.**

Unlike a bank loan or a credit card debt, a mortgage is what's called 'secured'. That means in return for lending you money, the bank uses the property as security for the mortgage. While 'security' may sound good, it's the lender not you that gets the security, as it means if you get into problems and can't repay, it has the right to repossess your home and sell it to recoup the money borrowed.

Not only that, but if it does repossess and the amount it gets from selling the home doesn't cover what you borrowed you'll usually still owe it the remainder. That's why ensuring you only borrow what you can afford is so crucial.

A Martin's Mortgage Moment

It's tougher than it used to be

The lack of available borrowing, since the credit crunch means lenders have become vastly more selective in who they lend to, to ensure those they deem to be the best customers get priority. Those seen as better customers are those with large deposits and with spotless credit histories.

In other words, whereas once lenders were salivating with glee at the thought of lending to anyone and everyone, and would throw money out there, now their fists are tightly clamped around every penny.

In the old days, good deals were shockingly available for those who were borrowing up to 125% of their property's value. Now that's changed, and often to get a decent mortgage you will need a deposit of up to 25% (perhaps even more) to secure it, and a good credit score.

That prices many out of the market and means serious saving, and a good repayment history, is often needed to begin with.

There is no one-size-fits-all deal. The choice depends on your current and likely future financial situation.

Navigating through the plethora of deals on offer can seem bewildering, but it boils down to a series of consecutive choices.

Choice Number 1: Interest only or repayment mortgage?

With an interest-only mortgage, your monthly payment does not chip away at your actual debt – it just covers the cost of borrowing the money. After 25 years of paying the interest on a £100,000 loan, you would still owe £100,000.

Whereas with a repayment mortgage, while it costs more each month, it has the big bonus that as well as covering the interest it pays off the original debt too, meaning you'd owe nothing at the end.

Unless you have a compelling reason, repayment is the way forward. It's the only option which guarantees you are actually paying off some of your debt every month. With an interest only mortgage, you just pay the interest, and should set up a method (eg, savings) to build up enough cash to pay off the actual cost of the property.

Some mortgages designed for first time buyers suggest you just pay the interest for the first couple of years and then convert to a repayment later on. That might work if you're struggling to get on the property ladder, but it's important to make sure you do shift to repayment when you can. The sooner you start paying off your mortgage the sooner you'll finish. There are a couple of exceptions which we'll get to in good time.

A Martin's Mortgage Moment

Interest only mortgages aren't bad

"Eh, what ?… that's not what you've said above. That's not the prevailing wisdom in every newspaper, what you going on about Lewis?"

All that's true, but it's over simplistic. While interest only mortgages aren't bad, they are risky. Risk is an important concept in finance; it's about taking a chance. The historic problem with interest only mortgages has been that most people who took them out did so without realising there was a risk. That is bad.

The point is the investment you use to pay off the capital on your interest only mortgage may soar, in which case it'd pay for your house plus more on top, or it may plummet in which case you need make up the shortfall.

It is possible for a detailed rational gamble on an interest only mortgage to pay off. Yet that gamble is beyond the scope of this guide. The reason most people are, and should be, cautioned against these mortgages, is planning, understanding and managing that gamble is complicated, and rarely something to risk your house on.

Beginner's Briefing

What is an interest rate?

Interest rates are the cost of borrowing money. So if rates are 1% that means if you borrow a pound over a year you'll repay £1.01. If rates are 44%, you'll need to repay £1.44.

While that's simple, what complicates the actual cost you pay is 'compound interest'. In other words, you're charged interest on the interest and over time this adds up.

The chart below shows you the impact, the first column is the amount of interest you'd pay if compound interest didn't exist – if you only paid interest on what you originally borrowed. The second is the interest on the interest.

Interest at 5% on £100,000 borrowed (assuming no repayments made)

Number of Years Borrowed	Total Interest Charged (no compounding)	Total Interest (with compounding)
1	£5,000	£5,000
2	£10,000	£10,250
3	£15,000	£15,760
4	£20,000	£21,550
5	£25,000	£27,630
10	£50,000	£62,890
15	£75,000	£107,890
20	£100,000	£165,330
25	£125,000	£238,630

As you can see, the longer you borrow for, the bigger the impact of compound interest, and a typical mortgage term is 25 years. If you can afford the higher monthly payments on a shorter term, in the long run, you will save serious cash.

How it works with mortgages

While the table shows the huge impact of compound interest, luckily, it never quite works like that with mortgages...

- **Interest only mortgages**

  If you have an interest only mortgage, the cost is pretty simple – if you've borrowed £100,000 at an interest rate of 5%, the cost is £5,000 a year though remember that means you still owe the original debt.

- **Repayment**

  On repayment mortgages it gets a bit more complex – your repayments are calculated so you'll have repaid all the debt and the interest over the term you agree (eg, 25 years).

  Yet this has a strange effect. In early years, your outstanding debt is larger so more of your monthly repayments go towards paying the interest. Gradually, as you reduce what you owe, the interest decreases.

  For example, on a £100,000 mortgage at 5%, after ten years you will have repaid £70,000 but only reduced what you owe by £26,100. Yet after a further ten years, paying another £70,000 now you've reduced the debt by a further £43,000 – much more because less interest is accruing each year. To see the details for your own situation go to www.moneysavingexpert.com/mortgagecalc

  Many people, once they realise this, then worry that if they ever change mortgage deal (remortgage) they will lose all the work they've put in to decrease what they owe. This isn't true, provided you keep the same debt and remaining mortgage term (ie, you have 14 years left to repay and you still try and repay in 14 years) it stays the same.

Choice Number 2: What type of deal do you want?

There are two main types of mortgage deal: fixed or variable.

A fix

Whatever happens to interest rates, your repayments are fixed for as long as the deal lasts – typically 2, 3 or 5 years. You're effectively taking out an insurance policy against interest rates going up.

Yet of course, if rates tumble your payments will not fall. It is sometimes possible to fix for 10 or even 15 years but such long term security is expensive. Most fixes revert to the standard variable rate on expiry (see below).

This protection from rate rises costs, so all other things being equal, a 3-year fix will have a higher rate than a 3-year variable. Then again, things are rarely equal and the balance of power between fixed and variable at any time depends on complex interactions – such as the market's view of long and short term interest rate trends.

✓ **PROS**

Certainty. You know exactly what your mortgage will cost. Your payments will not go up no matter how high rates go.

✗ **CONS**

Rates are usually higher than on discount products. If interest rates fall you will not see your payments drop.

Variable rates

As the name suggests, this means your mortgage rate can and usually will change over time. This tends to relate to what the UK's economic conditions are like.

In times of growth and inflation, interest rates tend to be increased to discourage spending. This is because it makes savings more attractive and borrowing costlier – meaning people are less likely to borrow to spend. In recession times, interest rates are decreased to encourage spending.

Variable rate deals fall into three categories:

1. Trackers

A tracker follows the UK Bank of England Base Rate. So if bank rate rises by 1 percentage point your mortgage rate rises by the same margin. But if it falls by 1 percentage point your mortgage drops by the same amount. Some trackers only run for a couple of years but you can get one lasting the life of your loan.

Beware the few deals that have what's called a "collar" – a minimum level below which the rate will not drop. When base rate fell below 2% during the credit crunch, some collars were invoked.

Most trackers revert to the standard variable rate on expiry (see below).

✓ PROS

You get the full benefit of all Bank of England rate falls – subject to any "collar".

✗ CONS

You get the full cost of all Bank of England rate increases.

2. Standard variable rates (SVRs)

The simplest and most straightforward option, though not always available to new customers. However, many introductory fixes or trackers revert to the SVR on expiry, so it's important to understand it.

Each lender offers an SVR (or rate with a similar name) which tends to roughly follow base rate. SVRs are generally two or more percentage points above base. As the base rate shifts up and down so lenders traditionally move their SVRs, although not always by the same amount. For example, they may only drop rates by 0.2% when the base rate drops by 0.25%, meaning they increase profits.

The problem is they don't have to follow base rate. They are allowed to move the rate simply at their own competitive whim, and there are many examples of this happening, massively hiking people's costs.

✓ PROS

Simple.

✗ CONS

There's no guarantee you'll get the full benefit of all rate changes as you're at the mercy of lenders hiking rates at their will.

3. Discount

These deals usually offer a discount off a tracker or standard variable rate (SVR). The discount tends to last for a relatively short period – typically 2 or 3 years.

The problem can be the way these deals are marketed and can make expensive deals seem cheaper than they are. For example:

Huddline Bank

This has a huge 2% discount for two years, but the discount is off an SVR of 7%. In other words, the rate you actually pay is 5%.

Cansistont Building Society

This has only 1% discount also lasting two years, but it is off an SVR of 6%. So the rate you pay here too is 5%.

So with different discounts the actual rate paid is the same. Therefore it's important to know both how big the discount is and what it's off.

It's also worth noting that you can get a discount off a tracker rate rather than the SVR, eg, if the tracker is base rate + 0.75%, and it is discounted by 0.5% for the first two years, you will pay base rate + 0.25% during that time.

✓ PROS

It's often cheaper than the underlying rate, such as the SVR.

✗ CONS

As you are sometimes linked to the SVR, you are at the mercy of lenders hiking rates.

A hybrid option – capped deals

Part variable rate, part fixed. The rate you pay moves in line with the base rate or SVR but there is an upper ceiling or cap which gives you some protection.

Just as a collar sets a minimum rate so a cap sets a maximum rate above which your payments will not go. As you might expect, these mortgages tend to be popular when people are frightened rates might soar.

✓ PROS

You benefit from interest rate falls and have some protection from interest rate rises.

✗ CONS

The cap tends to be set quite high, and the starting rate is generally higher than normal variable and fixed rates.

A Martin's Mortgage Moment

Choosing between fixed and variable

There is no right answer here. It depends on your circumstances and your priorities. A fixed rate is like an insurance policy against interest rates going up. That protection costs money, so other things being equal, unless there are exceptional circumstances, a 3-year fix will have a higher initial rate than a 3-year discount. However, the rate of the discount deal may go up or down.

It isn't all about what's cheapest

Shock, horror thought from the Money Saving Expert, but choosing a rate isn't purely about which is the very cheapest. Deciding whether to fix is a question of weighing up how important surety is for you. I tend to think of this as a "how close to the edge are you?" question.

Someone who can only just afford their mortgage repayments should not be gambling with interest rates, and therefore will benefit much more from a fixed rate as it means they'll never be pushed over the brink by a rate increase.

Those with lots of spare cash over and above the mortgage may choose to head for a discount, and take the gamble that it will work out cheaper in the long run.

Don't look back in anger. If you do decide to go for a fixed rate on the basis of security and afterwards look back with hindsight and realise a discount rate would've been cheaper, this doesn't mean it was the wrong decision. If you needed surety, remember, you got it.

As I love my analogies, let me give you one.

If I asked you to call head or tails on a coin toss and said I'll give you £10 if you win, but you only need pay me £1 if you lose, then you should do it. While the bet itself doesn't increase your chances of winning, the reward for winning is much better than the cost of losing. So if when we actually tossed the coin, you lost, the bet was still worthwhile. It's the same with picking a fixed rate.

Choice Number 3: Do you want flexibility?

Once you've worked out whether it's repayment or interest only, fixed or discount, decide whether you want a mortgage that flexes – this means getting functions that allow you to increase or decrease what you repay.

The real question here isn't about 'to flex or not to flex' but how much flexibility you want. Over the past ten years and more, as flexible mortgages have got popular many standard mortgages have had flexible features added. And as the more flexibility you want, the higher the rate usually, first consider what you need.

Can you overpay?

The most popular flexible feature is the ability to overpay which can result in clearing the debt substantially quicker, so you pay less interest overall (use the www.moneysavingexpert.com/mortgagecalc to see the impact) yet many standard mortgages allow you to do this.

However, they restrict the amount of money you can overpay – typically a maximum of £500 a month or 10% of the outstanding mortgage per year. Penalties if you go over these limits can be steep.

In some cases, although the extra money you pay is knocked off your outstanding debt for the purposes of calculating the interest you owe, in fact the lender keeps the money in a separate pot. You can draw on this in the future either by taking back a lump sum, or using the surplus to cover your monthly payments.

So check the situation and work out how realistic it is that you'll need to overpay beyond the amount usually allowed before plumping for flexibility.

Can you take payment holidays?

Be careful. Lenders don't let you play hooky from the goodness of their hearts. You will pay for it. Typically, borrowers arrange to miss one or two payments, and their monthly payments are recalculated to spread the cost of the payment you missed over the rest of the life of your loan. There could also be an extra penalty or administration charge on top.

SOMETHING A BIT DIFFERENT

So far, the focus has been on mortgages that are variations on a simple theme. You borrow a set amount of money, you pay back a certain amount every month, and your debt is the amount you borrowed minus the repayments you've made.

So far, so straightforward. But for ultimate flexibility there are two completely different types of mortgages that allow you to use your savings and/or the money which sits in your current account to reduce the amount of money you owe – often in conjunction with the fixed or discount rate offers described above.

Current account mortgages (CAMs)

As it says on the tin, this combines your mortgage and current account, to give you one balance. So if you have £2,000 in your current account and a mortgage of £90,000, then you are effectively £88,000 overdrawn. Your debt is smallest just after your salary is paid in, and it then creeps up throughout the month.

You make a standard payment every month which is designed to clear your mortgage over the term you have chosen. The extra money floating around in your account is like an overpayment, which should mean you pay the loan off much more quickly. Any extra cash savings can be added to reduce the balance further. Or you can transfer other debts like credit cards or personal loans to the account to take advantage of the lower interest rate.

✓ PROS

If used correctly, someone who spends less than they earn each month is effectively overpaying their mortgage every month and so should clear it more quickly, potentially saving them thousands of pounds. However, this is not unique to CAM mortgages, see 'Martin's Mortgage Moment' on page 18.

✗ CONS

You have to be very organised with your money. While a mortgage is always a debt, when linked to your current account, it is more obvious on a day-to-day basis and can create the feeling of being permanently overdrawn. Plus, the interest rates charged on current account mortgages are often higher than those on normal deals. To work well you need to have a reasonable amount of money coming into – and floating around – your current account.

Offset mortgages

An offset keeps your mortgage, savings and current accounts in separate pots. Yet as above, your savings are used to reduce – or 'offset' – your mortgage. So, if you've a mortgage of £150,000 and savings of £15,000, then you only pay interest on the £135,000 difference.

Again you make a standard payment every month, but your savings act as a permanent overpayment, wiping out more of the capital every month, helping to clear the mortgage early.

Plus, it's also a good deal tax-wise. This is because the interest earned on the £15,000 in a normal savings account is usually taxed.

But it's far better to pay £15,000 less interest in your mortgage so there's no tax to pay on it, plus the mortgage rate is likely to be higher than what you'd earn in a savings account so you're best off paying less interest on the mortgage. So these accounts are particularly good value for higher rate tax payers.

Warning! These mortgages are not for the financially disorganised. You also need a reasonable amount of money coming in every month or a decent amount of savings to make the most of their features.

✓ PROS

You are effectively overpaying your mortgage every month and so should clear it more quickly, potentially saving you thousands of pounds. Your savings and debts are kept separate so it's easier to keep track of your money. Tax efficient, especially for higher rate taxpayers.

✗ CONS

As with CAMs, the interest rate is higher than on more straightforward mortgages. So you need to have reasonably substantial savings – at least 10% or more of the mortgage amount – to make the sums add up. If you need to spend your savings for any reason, then your mortgage will become more expensive.

A Martin's Mortgage Moment

Flexible facts

Wooooah there. OK, offset and current account mortgages sound great. Yet there's a lot of hype mixed in with these flexible friends.

The decision boils down to two questions. Will you use all the extra features? And is the higher interest rate you'll pay offset by the benefit?

Don't believe the marketing

You need be especially careful with current account mortgage providers. They provide illustrations which show how many tens of thousands 'paying your salary into your mortgage' will save you. Yet this is a myth.

Check the numbers behind those illustrations and you'll see it always includes a fact similar to "you spend all bar £100 a month" – in other words you're overpaying by £100 a month. While of course this overpayment is beneficial, it's not unique to the current account mortgage.

In fact, the pure benefit of actually paying your salary into your mortgage account each month (if you take out the overpayment) is roughly equivalent to a 0.1% discount in interest rate, and these type of mortgages are a lot more expensive than that in the first place. Unless there's a very special cheap rate these should most often be avoided.

OTHER QUESTIONS TO ASK

Does the lender charge daily interest?

Daily interest means the amount you owe is recalculated every time you pay money off. This means you pay less interest over the life of the loan. With annual interest you don't get the benefit of 12 months' payments until the end of the year. It can make a huge difference to what you pay. If you had 10 years to go on your £115,000 mortgage, a 5.35% deal charging daily interest would actually be similar value to a rate of 5% where interest was calculated annually.

Are there any extended redemption penalties?

What happens at the end of any special deal? While most people accept they will be penalised for shifting mortgage or repaying during the initial period, some lenders continue to charge redemption penalties even after this – hence "extended". Thankfully, these are gradually dying out, but check anyway.

What happens if I need to move house within the mortgage term?

Many mortgages are now 'portable', so moving house doesn't have to involve a new deal which can be important if you have redemption penalties. However, if you need additional funding, be careful to choose the right product so that the end dates of your exiting scheme and new scheme are similar, enabling you to move both mortgages, if necessary, to secure a better rate. Having no penalties on the top-up sum can often be good a policy.

2 First time buyers – boost your ability to get a mortgage

The days when lenders threw out mortgages like sweeties are long gone. To get a decent interest rate doesn't just need a big deposit, it now takes a big deposit and a decent credit score.

Neither of these can be done at speed, therefore some will need to simply accept that a mortgage is either simply unavailable, or even if you can get one, you need to pay such a prohibitive rate it is unaffordable.

Step 1: Boost your credit score

A lender will want to know that you are likely to be a good profitable customer and make your repayments. It does this by credit scoring you to try and predict your behaviour. This is based on a raft of different data and each lender scores you differently.

These criteria aren't published, so it's impossible to pinpoint which lender wants what, though many mortgage brokers (see chapter 4) have a reasonable guide to which lenders are pickier.

However, if you've a poor credit history, there is now very little chance you'll get a mortgage. The 'sub prime' market which used to allow lending to those with poor credit is now effectively closed down, partly because much of the credit crunch was blamed on it.

Lenders are now much more selective in who they lend to as they have less money to dish out. Therefore, they want borrowers least likely to miss payments.

The credit scoring process is designed to weed just such customers out. It aims to predict your future behaviour based on your past. Therefore, ensuring your credit history looks as good as possible, and that your lender knows enough about you, helps.

What to do

- **Get on the electoral roll**
  If not, you're unlikely to ever get credit. Go to www.aboutmyvote.co.uk to register on the electoral roll or to check whether you're already registered. For anyone ineligible (mainly foreign nationals), send all credit reference agencies proof of residency & ask them to add a note to verify this.
- **Check addresses on your file**
  Get your credit file (see www.moneysavingexpert.com/creditrating for how to check for free) and ensure every active account registered (eg, current account), even if unused, has the correct address. Errors can trigger rejection.
- **Delink from past relationships**
  Write to credit agencies asking to be delinked from any ex you had joint finances with. This stops their credit history impacting your applications.
- **Amend errors**
  If you think your file's wrong, ask the lender to correct it. If it won't, add a *notice of correction* to your file explaining why it's unfair & complain to the Financial Ombudsman.
- **Cancel unused cards**
  Access to too much credit, even unused, is bad.
- **Build / rebuild your score**
  Poor scorers should apply for expensive (30%+) credit cards, spend a little each month, but ALWAYS repay in full to avoid interest. This should slowly improve your score. See www.moneysavingexpert.com/badcredit

What not to do

- **Don't miss payments / pay late**
  Set up a direct debit to make at least the min. repayment on credit cards so you're never late. Though try and pay more on top.
- **Don't make lots of applications together**
  Space out applying for anything that adds a footprint to your file (including car insurance, mobiles).
- **Don't do joint finances**
  It's not marriage or cohabitation but joint products (bank accounts or mortgages) that financially links a couple, so avoid if one has a poor history.
- **Never apply after rejection**
  Always check for errors on your credit files before applying for anything else. If not, even if you fix an error later on, all the footprints from rejected applications may kibosh your ability to gain credit anyway.

These are just the tip of the iceberg. For a full guide to boosting your credit score go to www.moneysavingexpert.com/creditrating.

Step 2: Get your deposit together

The days of deposit-less mortgages are long gone. You are going to need to get a substantial sum of cash together to get a property. Lenders require this both to prove you're solvent and have financial discipline but also as it means the loan is less of the property value, protecting the mortgage company if you are ultimately unable to repay.

To get a good mortgage you will often need up to 25% of the home's value as a deposit and more than 40% for a seriously cheap deal. It is possible to do it with less but the rate you pay can be much higher – if so, stop and consider whether it's right for you.

With lower deposits, rates increase and availability decreases, plus some lenders impose a "higher lending charge", which used to be called a "mortgage indemnity guarantee", when you borrow more than 90% of the property value (have 10% or less deposit).

This 90% figure is known as the Loan-to-value ratio (LTV). Even where there isn't a specific charge, many lenders offer cheaper interest rates if your LTV is below 75% and even better deals if it's below 60%. If you borrow at a high LTV, 90% or more, you should be looking at a lender that doesn't levy a higher lending charge as this will further add to your costs.

There's no easy shortcut to getting the cash – it may be saving up, money from parents, selling your car or an inheritance. No deposit = no mortgage.

Step 3: Examine your finances

First thing's first. This is a numbers game so before you do anything else, have a good look at your finances. Use www.budgetbrain.com to do a full budget to calculate what you can realistically afford to pay every month. Do your homework to find out what's available.

Historically, lenders simply multiplied your income to work out how much to lend you. Typically, a single person could borrow 3.5 times their single salary while a couple would be offered 2.5 times their joint salary.

Step 4: Special deals that help first-timers

As a big deposit isn't easy to raise the first time, there are a number of innovative schemes specifically to help first timers.

- **Short term interest only deals**

  Most mortgages should be on a repayment basis (see page 5), as this is the only guaranteed way to reduce your debt. But there are some first time buyer mortgages which have been designed to be interest-only for a few years only.

  This reduces the initial monthly payments but again means that you're only servicing the debt – no capital is actually being repaid during this time. So you still owe the same amount after those few years. The hope is that by the end of the period, your salary and the value of your property will both have increased, meaning you can afford to switch to a repayment deal.

- **Parent power**

  Many first time buyers rely on help from mum and dad for their deposit. But parents can be much more directly involved. A number of deals will also take into account parental income as well as the child's income, as long as they can still cover their own mortgage.

  To avoid tax complications the parents are not listed as owners, but they are liable for repayments and arrears. It's also possible for parents to guarantee just the extra portion of the mortgage above the amount covered by their child's income, or to undertake to cover repayments should the child default.

  Parents can also help their children without surrendering their cash. There are sometimes offset mortgages which will use parental savings to reduce the child's mortgage, while still allowing access to the cash if necessary.

- **Mates mortgages**

  Another route could be to buy a property with a friend. Lenders sometimes allow up to four people to get a joint mortgage although some are more generous than others with regard to lending multiples. Clearly, the pooled salaries increase your buying power, but remember you'll need a bigger property, which could take you into a higher price and stamp duty bracket.

  See www.moneysavingexpert.com/stampduty

  You also need to consider what would happen if one of you lost your job or wanted to sell your share. It's not something to be done lightly. Do not do this without sorting a legal contract between you of what happens and what your rights are. Too many people don't arrange it thinking "we're good friends" or even "we're lovers" and when it all goes wrong it causes a nightmare.

- **Shared ownership**

  You may also be eligible for one of the many shared ownership schemes available across the country. Under conventional shared ownership schemes, run by housing associations, borrowers buy a share of a property worth between 25% and 75% and pay rent on the rest, with the right to increase their share in the future.

  And there is sometimes additional help for 'key workers' like nurses, teachers and policemen, although the eligibility criteria varies according to local recruitment and retention priorities.

  Competition for all these schemes is and will be fierce but they're worth exploring. However, just because it's available doesn't mean it's the best route. Compare it to going it alone. For more information go to www.communities.gov.uk or contact your local authority and/or housing association.

A Martin's Mortgage Moment

Don't be too keen to get on the housing ladder

"Must own, must own, must own," has become a mantra of our age. I remember meeting a 21-year-old couple while filming a Tonight with Trevor MacDonald who were upset they weren't on the housing ladder yet.

Let's make this plain. Owning a house is great, but no necessity. Contrary to popular perception house prices can go down both in the short term and the long term. True, over the very long term it's unlikely, but no one can predict the future.

If you're buying a house to live in, the fact you won't need to pay rent really does help the equation. Yet don't starve to do it. Your overall finances are more important, make sure you can afford the house and definitely don't overstretch yourself – if you think it may be a little much, take a step back and pause. Not owning is better than getting reposessed. Better to wait a little until you're secure.

Remember renting isn't a crime. In some circumstances it's worse, but if house prices drop it's better. No one really knows, so don't panic.

3 Mortgages for the self-employed / contract workers

If you're self employed or would struggle to prove your long-term income (for example, you've worked abroad or you are on a temporary contract) then getting a mortgage is tough.

You'll need cast-iron proof of your income. This is easy for those who are employed as they can show pay slips or employment contracts, but much tougher if you work for yourself or do not have a permanent contract.

What you'll need to get a mortgage

You'll need rigorous evidence of your income, this is usually done in one of two formats.

- **Business accounts.** You want to be able to show preferably three years of accounts – though two can suffice. Usually, they need to be signed off by a chartered accountant.
- **Tax Returns.** If you can't show business accounts then two or three years' tax returns is the next best option.

You'll be assessed on profits not turnover, and as many companies try to minimise declared profits to pay less tax, this means it could be harder to get a bigger mortgage.

If this is likely to be a complex process then often using a mortgage broker (see chapter 4) will help the process as they'll know which mortgage lenders require what.

All this is fine for established businesses, but being brutally realistic, could mean those who have recently started working for themselves will simply not be able to get a mortgage. Or if looking with a partner who is self-employed, their income may not help you get a mortgage if it cannot be proved.

Lenders are looking at designing mortgages for the recently self-employed but until their products come to market and get the necessary seal of approval from the regulator, you may have to accept you cannot get a home loan if you don't have the necessary paperwork.

What about self-certification mortgages?

In 2009, the regulator, the Financial Services Authority, proposed that self-certification mortgages should be banned. With self-certification mortgages, for a higher interest rate, you didn't necessarily need any evidence of income and simply declared a figure yourself to get a mortgage.

There was evidence of abuse of the system by borrowers and some mortgage brokers, leading to people borrowing far more than they could afford, which is why they may be banned. Self-certification mortgages were sometimes dubbed 'liar loans' as a result.

No lender was offering self-certification mortgages as this guide went to press.

4 How to get a mortgage

Going solo

If you are confident you know what you want then there's nothing to stop you getting a mortgage on your own, though as explained in a moment, most people are better off using a broker.

However, as a start point, the internet can help you get details of different products and compare offers. For more information on a range of comparison sites, see www.moneysavingexpert.com/mortgageadvice. Newspapers also regularly publish best buy tables. Beware, some tables do not always include all fees payable.

Step 1 Select the mortgage deal or deals you fancy.
Get detailed quotes from the lender(s).

Step 2 Add up all the fees to get a figure for the total cost.

Step 3 Work out the cost over a set period.

Step 4 If you want to go ahead, apply to the new lender.
Often this can be done over the telephone or internet.

Step 5 Valuation and legal work.
This should take between 4 and 8 weeks.

Step 6 Completion.

A Martin's Mortgage Moment

Surprisingly, advice is worth it

Just going to your existing bank or building society is a waste of time. It will only look at its own products; whereas the best mortgage brokers view the entire market to find the cheapest deal. It's fine to ask it for its best offer, to find a benchmark, but don't ever just stop there.

Mortgage brokers speed it up and help…

I'm not usually a huge fan of financial advice. It's often costly, unwarranted, and as it concentrates on pensions, protection and investing, not the 'sort my finances' thing most people actually want.

Yet my tone changes with mortgages; the right brokers can quickly source a top product, offer an extra layer of protection if things go wrong, and carry more clout with lenders, easing the acceptance on otherwise unobtainable mortgages.

Many brokers negotiate exclusive deals with lenders that are simply not available to individual customers. And if you do it the right way, you can get the advice without paying for it.

The advice route

The mortgage market is so large and deals change so quickly that a specialist can really make a difference, but beware. Not all mortgage brokers are equal.

Since 2004, residential mortgage brokers have been regulated by the Financial Services Authority (FSA). The new regulations are welcome, but not without problems.

There are two key questions to ask a broker

1. ***"Are you whole of market?"***

This means, asking: "Will you look at all the UK's mortgage lenders to pick the best for me?" If not, forget it. Unfortunately, the FSA left brokers a loophole, allowing some to claim 'whole of market' status while offering only a panel of lenders, providing it's reviewed to include the 'best deals' roughly every two months. This is simply not often enough in the UK's fast-moving mortgage market.

The more advanced question: ***"Could you, right now, source a mortgage for me from any available UK mortgage lender?"*** should help cut the wheat from the chaff.

A Martin's Mortgage Moment

Always check non-broker deals too

A few lenders have always not offered their products through mortgage brokers. Yet when the credit crunch hit, more started to follow suit with their best deals. Under the regulations, 'whole of market' is technically defined as the whole of the 'available' market, therefore non-broker deals don't have to be included in the comparison, though some brokers will tell you about them.

While going to a broker is still the best start point, it's always worth checking the deals available elsewhere too. Of the major players that don't offer any deals through brokers, HSBC is often especially competitive, and ING Direct and First Direct are worth trying too.

In addition, virtually any company may decide to launch a product only available direct to customers, not via brokers.

Ultimately, this is a question of how much time and resource you can put in to supplement your broker-suggested best deal… it is worth doing a few checks, though. To keep up to date on this visit www.moneysavingexpert.com/mortgageadvice

2. ***"How will you make your money?"***

Brokers have two sources of income.

Commission. Almost all lenders pay brokers a 'procuration fee' worth a whopping 0.3% to 0.5% of the mortgage's value, rising to 1% for 'sub-prime' mortgages (for people with poor credit). On a £150,000 mortgage that's £450 to £1,500.

Fees. Brokers may also charge you a fee directly. No reputable broker will charge more than 1.25%, even for 'sub-prime' customers. Do not use anyone charging more. Obviously, the prime MoneySaving route is to go for a fee-free broker. But if you find someone you like, willing to spend time with you, with a low fee, go for it.

Previously, fees could only be charged on mortgage completion, now, providing brokers inform you at the outset, they can charge at any point in the process. However, even though it's legal, you should avoid any broker charging before completion as it can cause problems if things change later.

Step 1 Choose a broker. You should be told explicitly what advice will cost and when and how you will be expected to pay.

Step 2 Discuss your circumstances with the broker and it will recommend a deal.

Step 3 Check direct-only deals. See if you can beat your broker with deals it can't access. If you can, discuss it with your broker.

Step 4 Select a mortgage. The broker should make sure it meets your requirements and that the savings outweigh the benefits.

Step 5 You / your broker will make the application to the lender on your behalf.

Step 6 Valuation and legal work. This should take between 4 and 8 weeks.

Step 7 Completion.

The top brokers

There are lots of great local brokers and if you choose them carefully using the questions above, you should get an excellent face-to-face service. On the other hand the big brokers boast of greater market power.

Obviously, it's impossible to focus on every broker in the country, so let's stick with the main UK-wide mortgage brokers: Savills Private Finance, John Charcol and London & Country. All are completely 'whole of market' operators.

The only difference is in their charges…

The fees-free brokers
London & Country mortgages provides a telephone-only service, and as this is cheaper to operate, it can afford not to charge a fee, it just earns from the commission.

Fee-charging brokers
Both Savills Private Finance and John Charcol mortgages operate face-to-face services (as well as phone) and charge a fee.

Another option for the financially savvy

There are sometimes mortgage brokers which don't give any advice, but if you process the mortgage you choose through it you'll get some of the commission it earns as cashback, usually £100-£200 per £100,000 of mortgage.

Simply request the mortgage you want from a ready-made best buy list and you'll get cashback. This route's only for the very money savvy, so be extremely careful, better to get the right mortgage and no cashback than the wrong mortgage with cashback. Yet if you know what you want, it's better than going direct. Full info on the current cashback deals available at www.moneysavingexpert.com/mortgageadvice

A Martin's Mortgage Moment

Independence and integrity

This guide is sponsored by London & Country mortgages, that's the reason it is free. You will also see from the text on the previous page that it's my prime fee-free broker. So let me make something very plain.

This guide is written with absolute editorial independence. What's in it is purely dependent on my view of the best ways to save money and the sponsor's view on that is irrelevant. However, the reason I agreed to allow London & Country to be the sponsor, which enables this printed guide to exist, is because after detailed research into those brokers that offer coverage nationwide, London & Country has come out as one of the top for each of the last five years.

It's very important that this is understood and no one thinks it is the other way round, ie, it is recommended because it sponsors the guide. Like everything with MoneySavingExpert.com, the editorial (what's written) is purely about what's the best deal.

If London & Country no longer offers the deal it currently does, and either starts charging fees or stops being whole of market, I'd ditch my recommendation immediately. You can check if that's happened via an up-to-date article on mortgage brokers on the site. Just go to www.MoneySavingExpert.com/mortgageadvice.

5 Watch out for the hard sell on...

As the mortgage market has developed some lenders – and brokers – try to make more money elsewhere in the mortgage process. So be prepared for the hard sell on the following…

Mortgage payment protection insurance (MPPI)

Sometimes called accident, sickness and unemployment insurance (ASU), MPPI is supposed to cover your mortgage payments if you have an accident or become ill and can't work. However, MPPI policies are often expensive and generally have lots of complicated exclusions; for instance, self-employed people are usually not completely covered and there may be a relatively low maximum pay out. It's also important to note you may have to wait several weeks before the policy kicks in, and then it will usually only cover your mortgage repayments for one year.

Given these restrictions, MPPI may not be suitable for you, especially if your partner's income or your savings could realistically cover your share of the bills for at least a couple of months. Even if you do decide you want MPPI, you can probably get a cheaper deal by shopping around. For a full article on finding the cheapest see www.moneysavingexpert.com/mppi

Bundled buildings / contents insurance

Be very suspicious of deals which insist you buy your buildings insurance through your lender. While the amount quoted may seem reasonable in the first year, you are then trapped into accepting whatever premium increases they foist on you in subsequent years for as long as the mortgage lasts. Some lenders charge around £30 if you decline to take their insurance.

If you go elsewhere for your home cover, some seriously cheap deals are possible. By using cashback incentives some people get PAID to take our insurance. See www.moneysavingexpert.com/homeinsurance

Life cover from your mortgage seller

Would you buy a stereo from the man who cleans your windows? No, so don't assume just because someone sold you one financial product they will automatically get you a good deal on extra bits like life cover or other insurance. As with MPPI, check for best deals. In some cases you can save 50% on the life cover offered by your lender or broker. If your personal or medical circumstances have changed you may not be able to get cover at the same price, so occasionally it can pay to stick with an existing policy. But remember to cancel your old policy if you take out a new one. For a full guide on how to find the cheapest cover, see www.moneysavingexpert.com/mortgagelife

6 Don't forget the fees

Make sure when you do your sums that you take into account the full costs of buying a house and taking out a mortgage. You can try and minimise these – and some lenders will give you help towards them – but you can't magic them away.

If you can, keep back some of the money from your deposit to cover these costs. Realistically you might have to add them to your mortgage. But remember that means you'll be paying interest on the money for the length of the loan.

If you've followed the info so far your broker's advice should have been free.

But you should expect to pay your lender an arrangement fee. These have risen sharply over the last 12 months. They vary enormously but reckon on £500-£1,500. In some cases this is non-refundable even if the house purchase falls through. A couple of lenders also charge a separate reservation fee to secure a fixed-rate. This is always non-refundable and generally costs around £100-£200.

You should also expect to pay a valuation fee for a survey. This is to check a) the property exists and b) it offers the lender sufficient security for the loan. The cost depends on property value and your lender but assume around £250.

Then there are legal fees. Many lenders will contribute – although generally not in Scotland where the process is different – although in that case you would have to use a solicitor approved by your lender. If you have to pay for your conveyancing, you're looking at around £500-£750.

You will also have to pay stamp duty land tax to the government, which won't be included even if your lender will cover legal fees. For first-time buyers, there's none on properties up to £250,000 until March 2012. After that, and for everyone else (even now), there's none on properties worth up to £125,000 but you'll have to pay 1% of the value for properties worth between £125,001 and £250,000, 3% for those between £250,001 and £500,000, and 4% for those worth more. However, from April 2011 if your home is worth more than £1 million, you'll pay 5%. See www.moneysavingexpert.com/stampduty.

7 Buy to let

The explosion in property prices at the start of the millennium led to a buy to let boom of people buying homes and renting them out as an investment. Lots of people have been tempted to get involved because they feel comfortable with property.

But just because you own your own home doesn't give you the skills to make buy to let work. Ultimately the point of buy to let is to structure your finances such that you maximise your borrowing at the lowest possible cost. The stakes are high – and as the credit crunch years have shown – it's not for the faint-hearted.

If you want to buy a property to let out, you need a special buy to let mortgage. As with a residential mortgage you can chose between fixed and discount and so on, but when it comes to assessing how much you can borrow, the key factor is not how much you earn, but the likely rental income.

Borrowing limits

As a general rule lenders will not let you borrow more than 75% of the property value, and typically the rental income will need to be around 125% of the mortgage payment. So if your mortgage will cost you £600 a month, your expected rental income will need to be £750.

Certain lenders have relaxed these terms for some investors – especially those with multiple buy to let properties and therefore other sources of income – but the surplus gives an important cushion against periods when you have no tenant, known as 'voids', and helps cover maintenance and other costs.

As well as a hefty deposit, applicants are expected to own their own property. In addition, some lenders are unhappy providing buy to let mortgages on ex-council property, flats above a shop or in a high-rise block.

But for mainstream properties, the fierce competition in the buy to let market means that provided you meet the borrowing criteria, you can expect to get a mortgage at or only slightly above residential rates, although the arrangement fees are generally higher. Again, a broker can help you source a deal for your circumstances. All the major whole of market brokers offer buy to let mortgages. As before, you need to make sure the terms of the mortgage will suit your needs and you need to budget for the cost of taking it out.

Interest only

For most buy to let investors, the goal is to produce a rental income to pay the interest and other costs and make a profit on the sale, assuming house prices rise. For that reason, the majority of buy to let mortgages are interest-only loans.

This has two benefits. The monthly payment is much lower – making it easier to meet the stringent borrowing rules set out above. And it's also tax efficient because you can deduct the interest part of your mortgage payment from your rental income before you pay tax on it. This perk does not apply to the repayment element of mortgage payments.

Yet of course it also increases the risk if things go wrong and the property is no longer worth as much. Then you're in for a serious loss.

Gearing

This describes the relationship between how much you actually invest in a property and the amount of the lending. Being highly geared (more debt than capital) substantially increases the potential profits or loss.

This can also be used to increase your borrowing when house prices are going up. It is an important concept to understand, but please don't confuse this explanation of how it works with a suggestion that you should be doing this – getting it wrong is easy and can cause serious financial catastrophe.

You typically need to provide a 25% deposit for a buy to let property. If house prices increase then the bit you own is worth more too. Provided you are meeting your mortgage payments, lenders may let you use your portion of the property, or “equity”, to borrow more money.

Say you borrowed £75,000 to buy a £100,000 flat. If that flat is now worth £110,000, you can remortgage (get a new deal or ask the lender to give you more) it to release the extra equity.

As long as the rental income sums add up you could use that newly released money as a deposit on another buy to let property. And if it also increases in value, you can remortgage and release money again and buy a third property. In this way, in a rising market, it is possible to finance a string of buy to let properties without risking more of your own money than the first deposit. Increasing the size of your investment through borrowing is called ‘gearing’.

Clearly, gearing allows you to buy much more than you can afford in pure cash terms. In that way, it allows you to make a large return on a small stake.

Take the example above where you put down a 25% deposit to buy the £100,000 flat. If it increases in value to £110,000, then your stake has increased from £25,000 to £35,000, a return of 40%. Compare this to the situation if you had bought the house with £100,000 cash. That £10,000 increase would represent a return of only 10%. So in theory you have done much better by spending less.

But beware. It’s not just profits which are magnified – but losses too. If the same property fell by £10,000 then with the same gearing ratio, you’d have lost 40% of your money instead of the 10% lost by the cash buyer. And if you’ve bought lots of houses with only a small amount of capital the losses may be unaffordable – it’s not rare for buy to let investors to be repossessed or even find a knock-on impact on their own homes.

A Martin's Mortgage Moment

Is buy to let worth it?

Buy to let worries me. It's not wrong, but years of house price boom left everyone thinking 'invest in property and you can't lose'. Wrong! Property is a risk-based asset class like any other, or to paraphrase, house prices can drop like a stone, which eventually happened.

So consider the worse case scenario. You buy a house, no one rents it, and house prices crash. That is a dire situation, especially because of the gearing impact as explained above, which accelerates the loss.

Now that doesn't mean you shouldn't do it, just like buying shares, investing in property is about risk. You are trading the potential to make substantial gains with the potential to make substantial loses.

What really scares me is people who are highly geared (ie, lots of mortgage and little cash invested) and only have property investments. I won't say 'don't go for it', but be aware of the massive dangers of putting all your eggs in one basket.

8 Happy hunting

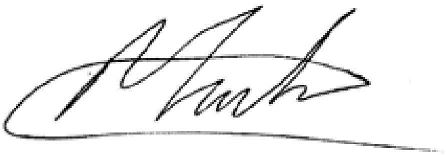
Getting your first mortgage – or even your second or third – is not the end of the story. Your circumstances may change, the deals available will certainly not stay the same. It's perfectly possible that today's perfect fit mortgage will be woefully out of shape in 2 or 3 years.

So, it's important to keep your eye on the ball – especially if you've chosen a deal which runs for a set period of time. You might even want to put a note in your diary a couple of months before your time is up.

Don't ignore it. Use it as a prompt to look again at your situation and research the market. And make sure that once you've tracked down the best deal, you take it. But don't forget to put another reminder in your calendar for the next time…

Happy Hunting.

We hope you save some money.



If you want more information, there are further articles at
www.MoneySavingExpert.com
and you can chat about the subject in the Mortgage section of the site's Chat Forum.

A word from the sponsor

This guide is sponsored by L&C (London & Country), the UK's leading **NO FEE** mortgage broker. L&C provides expert comment and best buy tables for the national press.

Unlike many other brokers, L&C charges **NO FEE** for the advice it gives and considers the whole of the mortgage market when it gives advice.

Its expertise has resulted in it winning many industry awards including the prestigious Money Marketing IFA of the year award for three consecutive years.

Whatever your situation, contact L&C for **FREE** advice on:

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YOUR HOME OR PROPERTY MAY BE REPOSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.

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PRIORITY ENQUIRY FORM

I have received the MoneysavingExpert.com guide and would now like FREE mortgage advice

Name: ....

2nd name on mortgage (if applicable): ....

Address: ....

.... Postcode: ....

Contact details:
Whom do you wish us to contact?: Applicant 1 ❑ Applicant 2 ❑ (pls tick)

Daytime Tel no: .... Evening Tel no: ....

Your current mortgage:
Value of property: £.. Amount owed on mortgage: £........................

Current lender: ....

Interest rate: ....% Monthly payment amount: £..............................

Do you have an early repayment charge? Yes ❑ No ❑ (pls tick)

If yes - how much is it? £.................................. When does it end?: / /

Your new mortgage:
Are you: Purchasing ❑ Remortgaging ❑ (pls tick)

Amount you wish to borrow: £.................................. For a term of: ....yrs

Simply fold and seal this Freepost enquiry form and post back to L&C. Alternatively, you can fax the form on 01225 442622 or call us on Freephone 0800 953 0598

Thank you
A L&C adviser will be in touch with you shortly.

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