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LandlordZONE

RENTAL PROPERTY KNOWLEDGE

Introduction—Buy To Let Mortgages

This edition of the LandlordZONE Newsletter looks at the some issues involved with mortgages and the current market conditions for buy to let.

The buy to let mortgage, introduced 11 years ago, has helped, along with the AST, to transform the rental market in the UK at a time when social and demographic changes demanded a big increase in rental accommodation. This has been good for the country and the economy.

However, during this time house price inflation has been unprecedented—the average house price has risen three-fold since 1991.

This has led to claims from some quarters that BTL landlords are to blame for the plight of first time buyers and that tax relief on buy to let mortgages should be removed.

Welcome

We're living in turbulent times. If you are interested in the broader picture from a renowned authority I recommend you read Alan Greenspan's timely biography—[The Age of Turbulence—Adventures in a New World](#).

Greenspan, chairman of US federal reserve for nearly 20 years, knows a thing or two about markets and has produced a very readable analysis.

Following the credit crunch of recent weeks, triggered by the US housing downturn

The five successive interest rate rises, now the credit crunch and so called “sub-prime” debacle in the US, have led to a slowing down of the housing market and to lenders being much more circumspect when it comes to approving loans.

Both these claims need to be challenged as far as genuine investor BTL landlord is concerned!

The speculators, some of whom have been buying to leave empty, and the growing number of second home owners, have no doubt had some effect on distorting the housing market, though this could change rapidly if we see a real downturn.

A recent CAB report claims that some landlords are using the possession procedure (Section 21) to avoid repairs, making their tenants live in squalor.

and the emergence of the so called “sub-prime” mortgage debacle, we're all now wondering if the UK housing market will follow suit.

A bleak warning by the IMF that Britain's homes are 40% overvalued—higher than the US market before it's collapse, at 9 times average earnings (up from 5 times in 2001) - does nothing to allay our fears.

But if the worst *should* happen, and it might not - then what?

Well, there's a strong letting market in the UK, a continuing housing shortage and low unemployment.

If you are not overstretched



The so called below market value (BMV) strategy now being advocated by some advisors (nothing new if you're a savvy investor landlord), if it is not applied ethically, is likely to be further grist to the mill to the critics of BTL.

Several high profile TV programmes out in the last week have been highlighting the seedier side of property investment and showing some of the horror stories on both sides—landlord AND tenant.

All of this does the image of the landlord no good whatsoever, as if it wasn't bad enough already in some quarters.

financially and you can manage your tenancies well, why worry about the value of your property in the short-term?

In fact there could be some real buying opportunities in the near future for those with the resources to add to their portfolios, but use good advisors and brokers.

All this is nothing new - we could be going back to normal conditions, where making money from property is about wise investments, managing tenancies well and making long-term gains.

Tom Entwistle, Editor

The Buy-to-Let Mortgage

It has been 10 years since the first buy to let mortgage came out.

In 1998 there were just 28,000 buy to let mortgage loans outstanding whereas the total now is 850,000, worth just under £100bn.

Ten years ago getting a good deal was hard and rates tended to be quite a bit above those on standard residential mortgages.

Many lenders stayed on the sidelines to see what happened, no doubt fearing that buy to let lending could only be done at low profit or with a

high level of bad debt. Their fears proved unfounded - repossession rates were actually no worse than on standard residential mortgages and in most cases better and showing good profits, so recently nearly all the big high street lenders have a buy to let product offering of some sort.

The 1.5% premium on the interest rate that used to be attached to a buy to let mortgage shrunk to about 0.2%. According to figures from the Council of Mortgage lenders there were 333,000

new buy to let mortgages in 2006 - just over 10% of all lending – and an almost 50% increase on 2005. This is only just short of the 350,000 mortgages taken out by first time buyers that same year. However, all this was before the credit crunch and the Northern Rock debacle. Although there's still demand for buy to let mortgages they're currently harder to get, suppliers are withdrawing many products, and to get good rates you are looking at higher fees and strict assessment criteria.



Buy to Let was an initiative of ARLA back in 1996 which has helped to transform the UK residential letting market. Read a summary of the new [The ARLA Review & Index of Returns on Residential Investment Q3 2007 - Sept 2007](#)

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It's still possible, but tougher to make profits

Getting a buy to let mortgage is much like getting any other mortgage with the two main additional constraints being the “rental cover to interest” and the usually tighter “loan to value” ratios.

Both of these have been relaxed in recent years (some would argue to a dangerous degree) as lenders have fought each other for new business. The rental cover to interest is the proportion by which the rent is greater than the interest that will be paid.

In general, you ought (for your own good) to ensure that the rent is equal to at least

125% of the mortgage interest, but lenders have increasingly relaxing this requirement.

The loan to value ratio is the amount of the mortgage loan divided by the house price.

Mortgage lenders tend to go up to a maximum of 80%, though some will do 85% or 90% and even more in one or two cases, though in general the higher the percentage, the higher the interest rate and the arrangement fee.

Some lenders have relaxed the rental cover restriction

to 100% of the interest, if you put up a larger deposit - say 25% of the equity.

With the property market currently in the doldrums and mortgage rates increasing, despite the possibility of a bank rate decline, making buy to let pay in the short term will not be easy.

This is despite good rental demand and many buy to let landlords looking to take advantage of property price declines and buy more.



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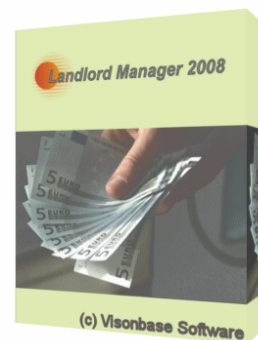
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Using a Broker

Around two thirds of all mortgages are now taken out via a specialist broker, with the figure for buy to let mortgages thought to be higher.

An experienced broker has the knowledge and the wherewithal to search the market for the best deals, relieving you of much of the administrative hassle.

Whether you get good advice from mortgage brokers is of particular concern to buy to let mortgage landlords as these mortgages are treated as commercial mortgages. They are still unregulated (unlike standard residential mortgages which come under strict FSA regulation) so it's important you use a broker you can trust and perhaps one that is FSA regulated for their standard mortgage business— recommendation is often the preferred route to a broker.

A good broker – who will be knowledgeable on letting and familiar with the nuances of each lender's criteria - will be looking to advise on the best deals that will work for you. It's in their interest to develop a good long-term working relationship where they can advise on purchases and new business and also on re-mortgaging as your portfolio develops.

A good broker will want to understand your investment strategy and the types of rental

property you deal with.

Long-term strategies work best, indeed it's getting impossible to make money on buy to let using a short-term speculation unless you buy well below market value.

A successful track record of buying and letting properties counts for a lot when it comes to structuring the deal, and the broker will want to know three other important pieces of information: (1) Do you know the market you are investing in? (2) Have you thoroughly researched the potential rental income and is this realistic? (3) Does the purchase price offer value for money?

The deal needs to stack-up on all three counts because, for example, you don't want to be paying a valuation fee if the rental figure is not achievable, or the sale price is well above the value of the property.

The next point to consider carefully is the amount of deposit you are willing to put down. The absolute minimum you are likely to get away with right now is 10%.

However, you just don't get something for nothing, so if you are looking for a 90% mortgage you are limiting your options in terms of suppliers and you are likely to be

paying top whack on set-up fees.

A 15% or more deposit is a far more realistic amount if you want to have a choice of options and secure a good mortgage deal for buy to let right now.

For your own financial security you should put more down if you can afford it, to ensure that the rental income (allowing for reasonable voids) stands a chance of covering your mortgage payments.

Good mortgages deals have without doubt become more difficult to secure following the recent credit crunch upheavals and the wariness of the institutions to get involved with anything that might be associated with the term "sub-prime".

One factor to consider is that many mortgage providers have had a very good year to-date and have achieved the loan targets they set back in January, so why should they go out on a limb now on marginal business?

It could be better to wait until the new year for some more competitive deals?

Additional information provided by Trevor Sharp brokers for:

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Review: [Renting—Guide to Tenant's Rights](#)—Lawpack

Those familiar with **Lawpack** publications will be aware of their wide range of high quality property related books, agreements, forms and legal kits. www.Lawpack.co.uk

Also, Tessa Shepperson, solicitor, author and website publisher www.LandlordLaw.co.uk has been published by Lawpack previously (Residential Lettings)

So it was with some confidence that I received this new book from **Lawpack** for review—I wasn't disappointed.

This is, as you would expect from Tessa, a comprehensive and up-to-date review of the

legal aspects of renting property.

Despite the title "The Essential Guide to Tenant's Rights" it's just as useful for landlords as it is for tenants—after all they are mirror images of each other.

At 312 pages this is no brief review, rather it's an in-depth and more importantly an up-to-date review of the whole process of residential lettings and the law.

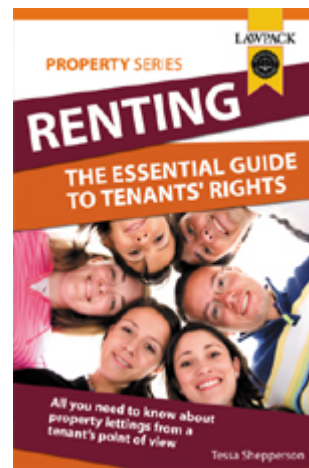
There have been some important changes to letting laws recently (and more to come by the way) so it's important that you keep up with all of these changes.

Starting off with a brief review of the English legal system, Tessa puts letting laws in England & Wales into context with the rest of the legal system and court procedures.

She goes on to cover tenancies (private and public sector) and the different types of housing tenancies, housing rights, tenancy agreements, housing benefit, repairs, harassment, eviction, and damage deposits.

For landlords and tenants, if you want to deepen your understanding of how the English letting system works this will be the best ten pounds you ever spent.

Tom Entwistle, Editor



Money Back Mortgages

In 2006 www.moneybackmortgages.com was set up to give consumers like you an impartial service where you can search for and arrange your next mortgage with the added benefit of receiving 50% of the commission received by us.

The website has proved particularly helpful for **Buy to Let landlords** who generally remortgage on a regular basis to lower their monthly mortgage costs. With interest rates increasing, here is a way of lowering your remortgage costs.

If you arrange your next Buy To Let mortgage through us you can expect to receive on average £337.09 per property**.

** This represents the commission payable to clients who have arranged a Buy to Let mortgage through us. Correct as of October 2007.

MoneyBackMortgages.com is a trading style of Quay FS Limited, which is authorised and regulated by the Financial Services Authority.

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Landlords should look beyond financing factors



Landlords should look beyond financing factors. A new study by TIC has revealed that 54 per cent of investors cite the size of the deposit as a leading factor in deciding whether or not to invest in a particular region, but numerous other studies suggest that it is in fact the long-term prospects of the area that matter most.

While lower upfront costs are undoubtedly enticing, landlords may find themselves losing out in the long run if they do not take heed of other factors. Just this week mortgage broker John Charcol has said that a long-term view should very much be a priority for prospective investors, and to take such a stance means considering other factors, such as local employment levels, amenities and the presence of good schools. Of the landlords polled by

TIC, 11.5 per cent said that the existence of regeneration projects in the area influences their investment decisions, but it is worth emphasising the importance of this factor, as recent research from the Investment Property Data-bank has shown that annual returns for residential property are consistently higher in regeneration areas.

Similarly, a look at case studies across the UK bears out the theory that employment trends are also crucial. A study of the Cambridge market found that by building new retail parks and commercial space, previously undesirable areas have attracted companies to relocate. This has created job opportunities, which in turn facilitated the arrival of high numbers of workers, significantly boosting demand for rental accommodation.

The presence of good schools cannot be discounted either, as a study from Halifax made startlingly obvious last year – house prices in areas with the best GCSE results are typically 12 per cent higher than the national average. Landlords should undertake a lengthy process of due diligence before investing in an area. Consider the long-term opportunities of any region, looking at regeneration projects, employment opportunities, local amenities, transport links, retail and leisure facilities and the existing and projected house price growth before committing to a project.

The sensible investor will undoubtedly take all these points into consideration, as well as the financial ones before taking the decision to invest.

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Be Careful Not to Over-stretch

Over the last few years some property investors and many notices have been buying up properties like there's no tomorrow. Egged on by some pretty unscrupulous advisors and with little thought as to where their tenants were coming from, they're now scrambling to let at the same time as scores of other investors. The reality is now beginning to dawn. Some developments are oversupplied, so tenant demand is low. Thus rent levels have dropped below the returns needed to make the investment viable, and the property value is probably considerably less than the

investor paid. Countless hard luck stories are now coming out into the open, and there could be more to come if tough conditions continue or even deteriorate further—you need really good advisors to steer you away from all this. Mortgage finance offers, where you could get 100% of mortgage interest in rent, are very risky because you need to ensure that you have a sufficient fall back in the event that rental income dries up due to voids, if interest rates rise or other unexpected costs arise. Many new landlords just don't understand that maintenance of a property let out

is often higher than on their own home or that it takes months to get a bad tenant evicted, plus all the costs to get the property back into a lettable condition. All this gives landlords with high borrowings very little room to play with before they have to heavily subsidise the shortfalls. Indeed, with gross yields at 6.1% (Paragon Buy to let Index July 07) and net yields probably around 4.5%, it does not take a genius to see that with base rates at 5.75% and mortgage arrangement fees starting at about £600, new entrants are already subsidising their investments.

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NPIA covers two areas of investment property: UK buy-to-let residential and UK commercial, both in the North East and North West of England, whilst EPIA specialise in overseas buy-to-let residential and commercial properties, predominately in major cities such as Berlin, Paris, Budapest, Warsaw, and more recently, the Cote D'Azur, Normandy and Brittany.

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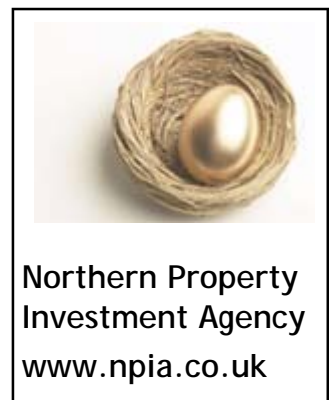
For further information go to our website on www.npia.co.uk, where you can register for property alerts, email us on info@npia.co.uk, or telephone Bernie or Craig on 020 8421 9801 for further information.

To Fix or Not?

Generally, fixed rates tend to be that much more attractive to landlords on a budget – those who may struggle a bit if the variable interest rate was to rise. Of course, the fixed rate will have a limited time period – two, three or five years being the most common. After that time you are back to the lender's standard variable rate - usually very uncompetitive.

The other option is discounts or trackers. Discounted rates are pegged at a pre-agreed margin below the lender's standard variable rate for a set period -again two, three or five years are the most common periods. If variable rates are your thing, look for a variable rate that tracks the Bank of England base rate, not the lender's arbitrarily set standard variable rate.

As with the fixed rate products, after the discount period ends, you will be back to the standard variable rate. Of course, the neat thing to do is to try to make sure you don't end up on the lousy standard variable rate – so make sure of the date when the rate ends - shop around in good time. Lenders thrive on inertia and people not realising there are better rates to be had than the standard variable rate.



Property Investor Show—SECC Glasgow—19-21 October 2007

The **Property Investor & Homebuyer Show** is the largest dedicated property event held in Scotland each year and returns to Scotland's premier exhibition venue - the **SECC Glasgow** - for a third year.

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What's in the News for Landlords?

A recent [Report by the Citizen's Advice Bureau](#) (CAB) claims that landlords are using the **threat of eviction** (under **Section 21 of the Housing Act 1988**) rather than respond to requests for repairs. The report by a CAB employee, Debbie Crow, which claims to be based on extensive research, is calling for changes to the legislation. The Housing Act 1988, widely acknowledged as being responsible for the resurgence of UK rental market, allows landlords to regain possession after the fixed-term without having to give a reason. CAB claim this is abused by landlords.

Removal of Tax Relief on Mortgage Interest. Following articles in the Guardian Newspaper on this topic - [Patrick Collinson](#) - arguing that investor landlords are enjoying this tax relief at the expense of first time buyers, the Institute of Directors (of all people) reported in the Financial Times - [Vanessa Houlder](#) - have now piled in with another argument: that landlords are enjoying this relief at the expense of other investors. This would be a devastating blow to some landlords. In fact the UK's property tax regime is not particularly generous when compared to some other G7 countries, and many allowances have not been increased for years - the Rent-a-Room allowance, for example, at £4250 pa has not been increased since 1992 when it was introduced.

The [Regulatory Reform \(Fire Safety Order\)](#) came into force October 2006 affecting landlords of commercial premises and also those owning purpose built and converted blocks of flats, plus some types of HMO. In the case of commercial premises the occupier as employer is generally responsible for carrying out a **Fire Risk Assessment** annually, but this responsibility is often shared with the landlord, especially where there are common areas. Landlords should ensure that risk assessments are carried out by whoever is responsible for management. Communities.gov.uk/

The [Royal Institution of Chartered Surveyors \(RICS\)](#) have published a report objecting to the unfairness of the government's **remove of empty rating relief on commercial premises**. The RICS are arguing that the measure will prompt many rating disputes as property rates are based on occupied property rents, turnover and trade. When a property is empty it's value may bear no relation to what it was when occupied, and may not re-let on such terms in the future. In addition, a multi-let building rated on a floor by floor basis is likely to produce an empty rating liability in excess of the value of the whole building.

Landlord Show—Birmingham NEC—6th December 2007

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Articles contributed to this
issue by **David**

Lawrenson, author of
[Successful Property
Letting - How to Make
Money in Buy to Let](#) the
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LandlordZONE® - Helping Landlords since 1999 - is a portal website for landlords, tenants & letting agents - a knowledge-base for practitioners, and a marketplace for buyers and suppliers. It gives Free access to all - and with around 1/2 Million visitors per month the site is a key focal point for the rental property industry. The site hosts the busiest rental property Question and Answer Forum for in the UK.

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