

Death knell sounded for interest-only mortgages

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Lloyds Bank is cutting back on interest-only mortgages as it seeks to mitigate the increased risks posed by such deals.

The bank, which is Britain's biggest mortgage lender and is part-owned by the taxpayer, will insist that customers looking to borrow more than £500,000 make capital repayments. People taking out interest-only mortgages through Halifax or Cheltenham & Gloucester will also have to pay a levy of 0.2 of a percentage point.

About one in five homeowners are estimated to be on interest-only deals. Millions of borrowers took out the loans during the housing boom and they are still popular among City workers and other borrowers who prefer to use bonuses to pay off the capital.

Aaron Strutt, Trinity Financial Group, another broker, said: "This will make it more difficult for creditworthy borrowers to take out a larger loan. People who expect bonuses often take out interest-only deals because quarterly bonuses can be used to repay the capital in chunks. These know that they will have to repay the mortgage at the end of the term."

Lloyds is also set to impose rigorous checks to ensure that interest-only borrowers have a suitable plan in place to repay their debt. It will no longer accept an expected windfall, such as inheritance or the sale of assets, as a suitable repayment vehicle. Instead, the bank will contact customers regularly to demand proof, such as annual statements, that they are building up an adequate pot of savings.

The changes will take effect at Halifax from today and at Cheltenham & Gloucester by the end of the month. Other lenders are expected to follow.

David Hollingworth, of London & Country Mortgages, said: "Borrowers without a watertight plan for repaying their debt will find it increasingly difficult to obtain an interest-only loan with any lender."

Lloyds said: "It is right that we review our approach to ensure that our products and procedures reflect the additional risks and responsibilities associated with interest-only lending, both to our customers and ourselves."

Separately, there was good news for borrowers yesterday with the release of Bank of England figures showing that the cost of short-term fixed-rate home loans fell to the lowest level on record last month. The average interest rate charged on a two-year fix for a 75 per cent loan dropped to 3.83 per cent — the lowest since records began in 1995.