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Buy-to-let returns top 10% a year

Investors are piling into the market as yields soar
James Charles Published: 5 February 2012



Landlords are securing double-digit annual returns in parts of London as the resurgence in the buy-to-let market continues to strengthen.

Research for The Sunday Times by findaproperty.com, the housing website, shows that parts of Greenwich, southeast London, offered gross rental yields of 10.2% in December. Leyton and Stratford, close to the Olympics site in east London, had gross yields of 9.4%.

Yields from buy-to-let properties nationwide (which show rental income as a proportion of property price) were 5.4% last year – the best since 2003 – according to Knight Frank, the estate agent. In contrast, the FTSE All-Share index yields 3.8%, UK government bonds pay 2%, and Bank rate is just 0.5%.

Liam Bailey of Knight Frank said: “Rents are rising, capital values are flat, and yields are improving, providing the strongest signal to investors in more than a decade.”

The buy-to-let market has seen unprecedented growth over the past two years, fuelled by a growing demand for rented homes. This is partly a result of the difficulties in securing mortgages in the aftermath of the credit crunch.

“In the long term, the buy-to-let market will remain strong, supported by structural factors such as the inability of people to get on the housing ladder,” added Bailey.



A survey released this week will show that first-time investors are piling into the buy-to-let sector in ever-greater numbers in search of strong yields, as returns on cash remain at an all-time low.

The survey of brokers by Paragon, the specialist lender, found that almost one in four loans went to first-time landlords in the final three months of the year, the highest level since 2006.

Lenders are seeking to capitalise on demand in the buy-to-let sector. Aaron Strutt of Trinity Financial, the broker, said: “Just a couple of years ago, banks were avoiding buy-to-let mortgages, but higher profit margins and strong demand have seen many change their tune.”

What mortgage deals are available?

The average interest rate on a buy-to-let loan has dropped from 5.31% to 4.79% over the past two years, according to moneyfacts.co.uk, the data firm. The number of deals available has soared from 243 to 486 over the same period.

The best-buy for those with a 25% deposit is a two-year fix from Nottingham building society at 4.19%, with a £1,299 fee.

Recently, a number of lenders have introduced deals for landlords with only a 20% deposit. The most competitive interest-only deal is from Leeds building society at 5.69% for a two-year fix. It has a £999 fee.

What returns can I achieve?

Lenders generally require rental income to be 125% of their standard variable rate (SVR) or your introductory mortgage rate, whichever is higher.

To qualify for the Nottingham deal, which has an SVR of 4.5%, you would need a yield of 4.2%, whereas borrowers taking the deal from Leeds, which has an SVR of 5.99%, would require a yield of 5.99% —more than the national average.

Calculations for The Sunday Times by London & Country, the broker, show somebody buying a £200,000 property in London with a £50,000 deposit (25%), and earning a rent of £917 a month, would receive a gross income of £10,999.

A borrower who took Nottingham's best- buy two-year fix would have interest-only mortgage payments of £524 a month, or £6,288 a year, leaving a profit of £4,711, or £393 a month.

After income tax at 20%, the net return would be £3,769 or £314 a month, a 7.5% return on the original investment, excluding any potential capital growth.

But the taxman wants his share

The taxman has warned homeowners who let properties during the Olympics that they must declare any taxable income — or face a penalty of up to 100% of the tax due, writes Alexandra Goss.

Accountants expect HM Revenue & Customs to step up checks on lettings adverts and websites during the Games to identify homeowners hoping to cash in on the event.

Paul Belsman at RSM Tenon, the accountant, said: “We know that HMRC checks adverts and websites for rental accommodation during big events and I suspect it will be even more vigilant during the Olympics.”

Mondaytofriday.com, a lettings site, said homeowners could charge £100 a night on average for a room during the event, depending on proximity to the venues and the facilities they offered.

Under HMRC's rent-a-room scheme, homeowners can receive up to £4,250 a year tax-free for letting a furnished room in their home to a lodger. If they make more than £4,250, or let out their entire property during the Games, they will need to declare this income on a self-assessment tax return, which must be filed by January 31, 2014.

HMRC said: “Around special events, such as the Olympics, we want to make sure that people who decide to let their properties, or parts of their properties, for short periods are declaring and paying the right amount of tax.”