Lenders impose interest-only limits

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Published: November 19 2010 17:43 | Last updated: November 19 2010 17:43

Private banks are becoming more cautious about granting interest-only mortgages on high loan-to-value (LTV) ratios, as concerns mount over falling house prices, brokers have warned.

Some lenders, such as Coutts and Barclays Wealth, had been willing to lend up to 80 per cent of a property's value on an interest-only basis. But mortgage brokers have found that these lenders are increasingly restricting the interest-only portion of any home loan to 70 per cent – and insisting that the portion of the loan above this amount be arranged on a capital and interest repayment basis.

"Of those happy to lend at higher loan-to-values, more and more often we are finding that they are restricting the interest-only portion to 70 to 75 per cent loan-to-value," said Nigel Bedford of Largemortgageloans.com.

Bedford said there are a number of reasons private banks are now more reluctant to lend high loan-to-values on interest-only, including the stricter capital adequacy requirements of the new Basel regulations and the forecasts of falling house prices over the next year.

According to Simon Gammon of Knight Frank Finance, private banks have also started to take a more active interest in the loan-to-value ratios within their mortgage portfolios.

"If they are concerned that the value of the property has fallen, they will phone clients up and say that they have to decrease their borrowing," he said. "We're telling clients to allocate some money for that just in case."

This tightening of lending policy reflects a similar trend in the mainstream mortgage market. Over the past six months, a growing number of high-street lenders have restricted their interest-only lending criteria in response to a review by the Financial Services Authority (FSA).

In July, the regulator said it would look at new rules for interest-only mortgages amid concerns that they were being used by borrowers who had no repayment vehicle in place. But some high-street lenders have pre-empted the regulator's proposals and introduced their own restrictions.

Most have limited interest-only borrowing to 75 per cent loan-to-value – with some lenders, such as **Lloyds Banking Group** and Coventry Building Society, no longer allowing interest-only repayments on loans above £500,000.

"It is much, much harder to get a relatively high loan-to-value deal done on an interest-only basis," said Melanie Bien of Private Finance, the mortgage broker.

High-street lenders are also demanding evidence of a borrower's ability to repay, as well as restricting the type of repayment vehicle that can be used. Last month, Woolwich became the latest lender to clamp down: it will no longer allow interest-only repayments on loans over 75 per cent loan-to-value and insists that a repayment vehicle must have been in place for at least 12 months before a mortgage is granted.

"Woolwich do not want to take on more interest-only mortgages because they already have such a massive exposure," said Aaron Strutt of Trinity Financial.

However, some high-street lenders will lend at higher loan-to-values if a borrower has an acceptable repayment vehicle in place. Nationwide Building Society will still lend up to 90 per cent loan-to-value on interest-only.

But, for wealthy borrowers who rely on bonuses, a private bank is often a better option as it can be more flexible. For example, for clients who need to borrow a high percentage of a property's value, brokers can arrange for part of a mortgage to be on a repayment basis with only quarterly or yearly "bullet payments" required. These can be set up to coincide with a borrowers' bonus income.

Bedford recently arranged a £1.7m private bank mortgage at 75 per cent loan-to-value for a wealthy client who receives a modest monthly salary with large quarterly distributions of profits from his law firm. The private bank wanted to limit the interest-only element to 70 per cent so Largemortgageloans.com arranged the additional 5 per cent loan on a three-year repayment basis, with capital overpayments to be paid quarterly after the client received his profit distributions.