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Loans and rates blow to buy-to-let landlords

Ruth Emery and Anna Mikhailova Published: 18 May 2014

Lending squeeze: Barclays (Dan Kitwood)

BUY-TO-LET investors face a double whammy of tighter lending rules on mortgages, which will dramatically cut the amount they can borrow, and a looming interest-rate rise that will eat into returns.

Woolwich, which has been one of the most generous buy-to-let lenders, will tighten its criteria tomorrow.

Currently the Barclays-owned lender calculates whether landlords can afford a mortgage by looking at the rate being offered. However, its stress test for applicants will now work out how much they can borrow using a flat rate of 5.79%, even if the mortgage interest rate is lower.

Ian Gray of the broker largemortgageloans.com said: "Someone taking out a two-year fix with £1,500 annual rental income would be allowed to borrow up to £437,689 today, but from Monday it will be only £248,705."

From tomorrow, only Clydesdale and Yorkshire banks will work out how much they are willing to lend using the actual interest rate of the buy-to-let mortgage. Most other lenders use a notional rate of 5% or more.

Meanwhile, the Bank of England said last week that it was in no rush to raise its base interest rate, but many economists believe it will do so, to 0.75%, by the end of the year.

Research by Platinum Property Partners for The Sunday Times shows that landlords may do best with multiple occupation mortgages (HMO).

On a £300,000 property with a 25% deposit, a landlord with a standard 3.59% buy-to-let mortgage makes an average 4% net annual return, while an investor with an HMO mortgage at 5.19% makes a 13% annual return.

If interest rates increase by one percentage point, this will leave the standard buy-to-let investor with a return of just 1%, while an HMO investor will still have a 12% return.

However, investing in HMOs is more complex and brings added risks. Landlords must comply with extra health and safety measures and may need a licence from the council, with fees ranging from £500 to £800.

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