Euro crisis may add 1% to your mortgage

Unrest is already pushing up costs, so consider fixing a rate now, writes **James Charles**

HOMEOWNERS should prepare for a sharp jump in mortgage rates next year, which could add more than £1,000 to average annual repayments, because of the threat of a second credit crunch.

Sir Mervyn King, governor of the Bank of England, said last week that the escalating crisis in the eurozone was "exceptionally threatening" to UK banks.

There was already evidence "that some banks may be starting to pass on higher funding costs to household and corporate customers through higher prices", the Bank said.

Fears about the exposure of European banks to the sovereign debt crisis have led to a steady rise in bank borrowing costs. Three-month Libor, the interbank rate, which indicates the wholesale cost of borrowing to fund new mortgage lending, hit 1.04% last week, up from 0.89% in September.

Ray Boulger of John Charcol, the broker, said: "One major UK lender has seen the margin it is charged above Libor jump from 3% to 5%, which it will have to pass on to borrowers in higher loan rates."

Economists said that a worsening of the crisis could see wholesale rates leap overnight. Jonathan Loynes of Capital Economics, the consultancy, said: "A serious escalation of fear in the banking sector could see these rates quickly rise. In such a situation, you can imagine that mortgage rates would soon follow suit."

He warned that a new credit crunch could push up the average mortgage rate, currently 3.61%, by one percentage point to 4.61%, adding £1,330 to the annual cost of a typical £200,000 repayment loan.

"Rates could rise by rather more than that if a severe credit crunch took hold of markets," Loynes added.

Brokers reported last week that mortgage lenders were continuing to raise interest rates on tracker and fixed-rate deals at short notice.

The Mortgage Works, part of Nationwide building society, raised some fixed rates by 0.5 points. ING Direct and Skipton building society increased fixed and tracker rates by 0.2 points while Santander added 0.1 points to its two-year trackers.

Moneyfacts, the comparison site, said that in the past two months, Santander and Northern Rock raised mortgage interest rates four times, while Halifax, the biggest lender, announced six rounds of increases.

Ian Gray of largemortgageloans.com, the broker, said: "We haven't been this worried about the availability of mortgage funds since the last credit crunch in 2008."

Book into a rate now

Borrowers who will need to remortgage in the coming months should try to book into a deal now, before rates rise even further. David Hollingworth of London & Country Mortgages, the broker, said: "It is clear that mortgage rates are only going upwards. If you are coming to the end of a deal in the next few months, it would make sense to book into a rate."

Many lenders allow you to secure an interest rate three months before you need to draw down the loan. HSBC, ING Direct and Yorkshire building society allow borrowers to reserve a rate up to six months in advance.

Most, though, charge a non-refundable booking fee. ING Direct levies a £195 fee, while Yorkshire charges £199.

Borrowers can reserve a rate with Woolwich, Barclays' mortgage arm, without drawing down until the end of May. It does not charge an upfront fee, but if you decide not to go ahead with the loan, there is a withdrawal fee of £150.

The current best-buy five-year fix is from HSBC at 3.28% for borrowers with a 40% deposit. It has a £1,999 fee. Those with a 25% deposit should opt for Yorkshire building society's five-year deal at 3.49%, which has a £300 arrangement fee on top of the £199 upfront booking fee.

Best-buy rates

Lifetime tracker
HSBC
£999 fee
40% deposit
2.39%
(1.89 points above Bank rate)

Five-year fix
HSBC
£1,999 fee
40% deposit
3.28%

Source: Moneysupermarket.com

Consider ditching your standard variable rate (SVR)

About 40% of borrowers are on SVRs, to which they are reverted at the end of a deal.

Nationwide, Halifax and Cheltenham & Gloucester customers on historical SVRs linked to Bank rate are not at risk of a rate rise, as experts expect Bank rate to remain flat for up to three more years. However, SVRs without this link could go up. Last month, Lloyds Banking Group raised the SVR for Bank of Scotland, hitting 175,000 customers. Handelsbanken, the Swedish bank, also raised its SVR.

Be wary of discounts

Some of the most competitive mortgage rates are discounts pegged to a lender's SVR, rather than Bank rate. Last month, HSBC introduced a deal for those with only a 10% deposit, pegged at 0.5 points below its SVR, so 3.94%.

Holmesdale building society has a two-year tracker at 1.99%, or 2.9 points below its SVR, with a £999 fee for those with a 25% deposit.

However, brokers urged borrowers to be cautious. Aaron Strutt of Trinity Financial Group said: "Unlike trackers, which are pegged to Bank rate, lenders can raise their SVR at any time, putting borrowers at risk of higher payments."

British mortgages depend on the future of the eurozone