You can afford your mortgage now, but what if…?

The **Money Advice Service** is here to help you manage your money better. We provide clear, unbiased advice to help you make informed choices.

We try to ensure that the information and advice in this guide is correct at time of print. For up-to-date information and money advice please visit our website – moneyadviceservice.org.uk.

About this guide

This guide is for you if you are taking out a mortgage. You need to think about how to afford the payments if things change.

When you read it you will know:

- in what circumstances your payments may change, and
- what you can do to prepare yourself.

Contents

How to repay your mortgage

Taking out a mortgage is one of the biggest financial commitments you can make, because of the amount you borrow and the time you take to repay it.

You may be able to afford the repayments now. But if you borrow a large amount over a long period think what may happen if, for example, your income falls or you lose your job. Or what if interest rates rise and your monthly repayments go up?

Bear in mind that a mortgage is a loan secured against your home, so if you fall behind in your mortgage payments, the bank or building society can sell your home to get back its money.

See the *Jargon buster* on page 12 for an explanation of some words you may come across when taking out a mortgage.

For more about mortgages, go to our website moneyadviceservice.org.uk/mortgages.

You can choose to repay your mortgage in the following ways:

- **repayment** – your monthly payment is split between paying off the loan and paying off the interest you owe on the loan; or
- **interest-only** – your monthly payment pays only the interest charges on your loan, and you must arrange some other way to repay the loan. (This will usually mean having an investment or savings plan to build up a lump sum to pay off the mortgage when the term ends); or
- a **combination** of the two.

Mortgage term

You can choose the length of time over which you pay back your mortgage – the 'term' – to suit you as long as the lender agrees you can afford it.

With an interest-only mortgage you pay the same each month to the lender whether the term is long, say 25 years, or short, say 10 years. If you plan to pay off the loan with an investment or savings plan, you will need to make sure the term is long enough for the plan's value to grow.

With a repayment mortgage over a shorter term, you'll have higher monthly payments but pay less in total. With a longer term, you'll pay less each month but more in total.

It's not a good idea to have a mortgage term that continues past the age you plan to retire unless you're sure you'll be able to afford the payments then.

Key points

- Use our online **budget planner** to help you work out what you can afford – see moneyadviceservice.org.uk/budget.
- Think about whether you need a fixed rate mortgage so that you know your payments will stay the same for a set period – but don't forget that if rates fall, your payments won't.

Key things to think about

You can afford your mortgage now, but think about how you'd manage if your, or your partner's, income fell or if interest rates increased.

How your income could fall

Your income could fall if you or your partner:

- lost your job(s), or had to take a drop in income
- stopped work to have a child or to look after a dependant, or
- became ill and couldn't work.

How your mortgage payments could go up

Interest rate increases

Unless you have a fixed rate for the full term of your mortgage, the interest rate you are charged can go up.

Mortgage interest rates are at a historically low level, but they may rise and your lender will usually apply some or all of the rise to your mortgage payments.

In the past, interest rates rose rapidly, from 7.5% to 15% in just a few years. Interest rate rises could increase your monthly payments considerably, making them difficult to afford.

Special rates ending

Often, special rates are for a set period only (three years for example), so when this ends your payment will change – it is likely to be much higher.

These examples show how different interest rates can affect your payments.

Example 1: repayment mortgage

You borrow £100,000 over 25 years on a repayment mortgage, initially at a rate of 4%:

Interest rate	Monthly repayment	Increase from 4%
4%	£528	-
6%	£644	+£116
8%	£772	+£244
10%	£909	+£381

Interest calculated monthly

Example 2: interest-only mortgage

You borrow £100,000 over 25 years on an interest-only mortgage, initially at a rate of 4%:

Interest rate	Monthly repayment	Increase from 4%
4%	£333	-
6%	£500	+£167
8%	£667	+£334
10%	£833	+£500

Interest calculated monthly

Don’t forget that rates could go higher than those shown here.

Key points

- Use our online **mortgage calculator** to help you work out what you can afford now and what your mortgage payments will be if interest rates rise – see moneyadviceservice.org.uk/mortcalc.
- Consider taking out insurance to help you pay your mortgage if you, or your partner, lost your job or became critically ill. But first find out about any restrictions for paying a claim.
- Think about setting up a savings account to help pay your mortgage in case of emergencies, and use our **savings calculator** to help you meet your savings goal – see moneyadviceservice.org.uk/savingscalc.

Take our online **health check**. Answer some straightforward questions and get your personal action plan to help you with your money must-do's and longer-term goals.

moneyadviceservice.org.uk/healthcheck

When deciding how much to borrow:

Check that you don't overstretch yourself by borrowing the maximum on offer. Just because you can afford it now doesn't mean you can afford it in the future. Use our **mortgage calculator** to work out what your mortgage payments will be if interest rates rise – see moneyadviceservice.org.uk/mortcalc.

Check that you get keyfacts® documents from your adviser or lender. Read them because they contain important information that the firm must give you about their service and the costs and features of the mortgage. They'll also tell you how much your payments will increase if the interest rate rises by 1%. Remember that rates can rise by more than this.

Check that you understand how the 'repayment' and 'interest only' options work, and what you must do to ensure you pay off your mortgage by the end of the term.

Check that you understand the interest-rate deals on offer and how they work. Make sure you know when a special deal will end and what will happen to your payments when it does (they are likely to be higher than before).

Your questions answered

Question:

How can I choose a savings account to build up an emergency fund?

Answer:

There are lots of savings accounts with varying interest rates and features. You should choose one where you can get at your money quickly when you need it.

For information on bank accounts, get a copy of our **Your bank account** guide – see *Useful contacts*.

You can compare savings accounts including cash ISAs using our online **comparison tables** – see moneyadviceservice.org.uk/tables.

Question:

Who should I talk to if I can't pay my mortgage payments?

Answer:

Talk to your lender as soon as you get into difficulties or think you might struggle to meet your payments.

They will have a set procedure for dealing with your situation. For example, they may be willing to accept less than the full monthly payment for a time, but this will depend on your circumstances.

Question:
Can I get help from the state?

Answer:

You may qualify for state benefits to help you pay your mortgage. Even so, you're only likely to receive help in certain circumstances and after an initial waiting period. If you do qualify for state benefits:

- payments will only cover the 'interest' part of the mortgage; and
- payments will only cover the interest on mortgages up to a certain limit. If your mortgage is above this limit, you will have to pay the interest on any amount over this limit yourself.

To find out the current limit, waiting period and more information, contact your local Jobcentre Plus (details in the Phone Book).

Find out about tax credits, such as the Working Tax or Child Tax Credits – see *Useful contacts* on page 15.

Question:
What insurance can I get to help me pay my mortgage if I lose my job or become ill?

Answer:

There are different types of insurance to cover you in case of redundancy, critical illness or an accident. Consider these but make sure you understand how and when they will pay out as there are restrictions.

Make sure you understand the limits of any policy and how it protects you. Ask a professional financial adviser for help if you are unsure.

For more about insurance, read our **Insurance** guide or visit the **Your money** section of our website – see *Useful contacts* on page 15.

Question:

Where can I get advice on the right mortgage deal for me?

Answer:

You can get professional financial advice from mortgage advisers on the high street or online.

Make sure they're regulated by the Financial Services Authority (FSA), the UK's financial services regulator, or are agents of regulated firms. This means they must meet certain standards the FSA sets and you are protected if things go wrong.

Question:

Where can I get more help?

Answer:

Whether you're buying your first home or want to change your mortgage, our trained advisers can help you with your questions over the phone or face to face. Call us on 0300 500 5000.

You can read more about mortgages at moneymadeclear.org.uk/mortgages, and our online **comparison tables** can help you shop around – see moneyadviceservice.org.uk/tables.

Next steps

Protect yourself against the risks of changes in your circumstances or interest rate rises.

Step 1	Plan your budget based on what you might have to pay in future as well as the initial cost of a mortgage. Don't forget to include all your household expenses, such as buildings and contents insurance premiums and council tax. This will help you decide how much you can afford to borrow. Use our online **budget planner** – see moneyadviceservice.org.uk/budget.
Step 2	Check what benefits your employer will provide if you become ill and can't work for a long time. Find out if you're eligible for tax credits – see *Useful contacts* on page 15.
Step 3	Put some money aside to help you in emergencies. For example, if you lost your job but had some savings, you would still be able to pay your mortgage and bills for a while. Use our **savings calculator** to help you work out how you can meet your savings goal – see moneyadviceservice.org.uk/savingscalc.
Step 4	Work out how long you could live on your savings if you lost your job. You may want to think about getting insurance to protect your mortgage payments, but make sure you understand its limitations.

Jargon buster

Some key words and phrases explained.

Agreement in principle
A certificate that some lenders give you, showing the amount they will probably be willing to lend you. This isn't a guarantee, but can be helpful when dealing with estate agents.

APR
Annual percentage rate of charge – this shows the overall cost of a loan each year, taking into account the term, interest rate and other costs.

Buy-to-let mortgage
A loan you take out to buy a property that you intend to rent to tenants.

Capital
The amount you borrow to help you buy your home.

Capped mortgage
A mortgage with a maximum limit on the interest rate you will pay during the deal period.

Deposit
The amount of money you put into buying a home (not including the money you are borrowing).

Discounted mortgage
This has a lower variable rate of interest for a set period, then the rate increases.

Early repayment charge
A charge you may have to pay if you pay back a mortgage early (including if you move to another lender).

Fixed rate
An interest rate that is fixed (in other words it doesn't move up or down) for a set time.

Income multiple
The number by which a lender multiplies your earnings to find out how much you can borrow.

Interest
The charge that lenders make when you borrow their money.

Interest-only mortgage

A mortgage in which you pay only the interest charges of the loan each month. You are not reducing the loan amount (the capital), and you must repay this in some other way.

Interest rate

The figure that decides how much interest you pay. It is usually linked to the Bank of England's rate and can move up or down.

keyfacts® documents

Standard documents that all regulated lenders and advisers must give you. The documents explain their services, costs and details of the mortgage you're interested in.

Loan-to-value

The amount of money you want to borrow compared (as a percentage) to the value of the property.

Mortgage

A loan secured on your property. If you don't keep up the mortgage repayments, your home may be repossessed.

Mortgage adviser

A mortgage adviser helps you get a mortgage from their available range. They may recommend a mortgage or give you information to help you choose.

Only firms and their agents that are regulated by the Financial Services Authority (the UK's financial services regulator) should give advice about mortgages. Check the FSA Register to see if they are regulated – see *Useful contacts* on page 15.

Remortgaging

Changing your mortgage for a better deal, without moving home.

Repayment mortgage

A mortgage in which you pay off both the loan (capital) and interest at the same time.

Secured

When a loan is 'secured' on your home, it means the lender can repossess your home and sell it to get its money back if you don't keep up your repayments.

Standard variable rate mortgage

The lender's normal interest rate – ie without any discounts or deals.

Term

The length of your mortgage, normally expressed in years.

Tracker mortgage

A mortgage with an interest rate linked to a particular base rate and moves up or down with it.

Useful contacts

Money Advice Service

For advice based on your own circumstances or to order other guides

Money Advice Line: 0300 500 5000
Typetalk: 1800 1 0300 500 5000

Calls should cost no more than 01 or 02 UK-wide calls, and are included in inclusive mobile and landline minutes. To help us maintain and improve our service, we may record or monitor calls.

Other Money Advice Service guides

- Dealing with your mortgage shortfall
- Getting financial advice
- Making a complaint
- Problems paying your mortgage
- Your bank account

For more titles, call us or go to **moneyadviceservice.org.uk/publications**

On our Money Advice Service website you can find:

- a **mortgage calculator** to help you estimate your monthly mortgage payments
- **comparison tables** for mortgages, savings accounts and mortgage payment protection insurance
- a **budget planner** to help you work out if you have enough money coming in to cover your bills
- a **savings calculator** to help you work out how you can meet your savings goal, and
- a **health check** to help you build up some good financial habits and reach your goals.

Go to **moneyadviceservice.org.uk/interactive**

Call rates to the following organisations may vary – check with your telephone provider.

Financial Services Authority (FSA)

To check the FSA Register, or to report misleading financial adverts or other promotions.

0845 606 1234
Minicom/textphone: 0845 730 0104
www.fsa.gov.uk

Other organisations that can help you

Association of British Insurers (ABI)

For information on insurance products.

www.abi.org.uk

Council of Mortgage Lenders (CML)

For guides on mortgages and home buying in England, Wales or Scotland.

www.cml.org.uk

Directgov

For information about tax credits and state benefits.

Tax credits helpline: 0845 300 3900
Textphone: 0845 300 3909
www.direct.gov.uk/money

Ethical Investment Research Service

Information about product providers and other sources that provide ethical investments.

www.yourethicalmoney.org

Finding a financial adviser

Unbiased.co.uk

For mortgage brokers or independent financial advisers in your area.

www.unbiased.co.uk

Institute of Financial Planning

Financial planners can help you achieve your goals by planning your finances.

www.financialplanning.org.uk

My LocalAdviser

For a mortgage, insurance or investment adviser in your area.

www.mylocaladviser.co.uk

The Personal Finance Society

For financial advisers in your area.

www.findanadviser.org

Complaints and compensation

Financial Ombudsman Service

Resolving complaints.

South Quay Plaza
183 Marsh Wall
London E14 9SR

0800 0 234 567 or 0300 123 9123
www.financial-ombudsman.org.uk

Financial Services Compensation Scheme (FSCS)

For claims against your adviser or lender if they have stopped trading.

7th Floor Lloyds Chambers
Portsoken Street
London E1 8BN

0800 678 1100 or 020 7741 4100
www.fscs.org.uk

the Money Advice Service™

This guide is part of our buying a home series.

Other titles in this series include:

- Dealing with your mortgage shortfall
- Problems paying your mortgage
- Sale-and-rent-back schemes

All our guides are available from:

Our website
moneyadviceservice.org.uk

Money Advice Line
0300 500 5000

If you would like this guide in Braille, large print or audio format, please call us on 0300 500 5000 or Typetalk on 1800 1 0300 500 5000.

Calls should cost no more than 01 or 02 UK-wide calls, and are included in inclusive mobile and landline minutes. To help us maintain and improve our service, we may record or monitor calls.

June 2011