

Mortgages

The Types Available

The mortgage industry has expanded the types of mortgages and interest rate options that can be offered to a client and the following is a simple description of the 3 main types and some of the interest options.

- Capital Repayment

Monthly repayments consist of one part capital and the other part is interest. The amount outstanding gradually decreases over time, until at the end of the term the full amount has been paid off. At the start of the mortgage the majority of a monthly payment is interest, and at the end it is capital.

- Interest Only

The Monthly repayment is interest only, and the mortgagee is expected to be able to find an additional source of money to pay off the mortgage at the end of the term. At the moment this is often an ISA or Pension plan, but the client may have other additional sources of income in future years.

- Offset

There are an increasing number of lenders that are offering an offset mortgage (Smile/Woolwich/Virgin/RBS). These mortgages use savings to offset the mortgage. For example, if a mortgage was £200,000 and the client had savings of £10,000, then the interest would only be calculated on the difference of £190,000. This reduction in interest can be significant over time. Most lenders also calculate interest on a daily basis, so every penny in an account can save money. In addition there is no interest paid on savings, so there is no tax to pay on any interest.

- Interest Rate Options
 - Fixed rate mortgages are set at a rate at the start of the term (generally 2-5 years) and do not change during the term. The advantage is if the rates rise, then the fixed rate does not, but the reverse is also true. An excellent mortgage if the control of cash flow is important. Fixed Rate mortgages are often limited in availability and can have additional charges and penalties.
 - Variable rate mortgages usually fluctuate in line with the Bank of England base rate.
 - Discount rate mortgages allow the client to pay a discounted variable interest rate for a fixed period.
 - A tracker rate follows the Bank of England base rate at a set margin (i.e. 1%).