

## SPECIAL REPORT: FIRST-TIME BUYERS AND AFFORDABILITY

## First-time buyers hit by double whammy

- New first-time buyers face double whammy of house price and rate rises
- Higher house prices alone add £75 to typical first-time buyer monthly costs compared to last year. Interest rate increases bring this up to almost £120
- Locking into a fixed rate loan this time last year would have saved a typical first-time buyer £170 to date, with further monthly savings of £50 at current mortgage rates
- More first-time buyers choose longer-term and interest-only mortgages which can cut more than £300 off monthly payments

Nationwide Building Society has released a report showing the effects of interest rate and house price rises on first-time buyers.

**Commenting on the figures Fionnuala Earley, Nationwide's Chief Economist, said:**

"As interest rates have increased to their highest level in over five years, the question of affordability again raises its head. House prices alone increased by just over 10% in 2006 adding almost £14,000 to the cost of a typical first-time buyer property, but three interest rate rises in six months add considerably more to the borrowing costs for this already struggling group.

"Compared to a first-time buyer entering the housing market in December 2005, a first-time buyer today would have to borrow more money, raise a larger deposit and pay higher interest rates than at this time last year. A typical first-time buyer entering the market now would face monthly payments around £120 higher than if they entered this time last year. On top of this they would have had to find almost £700 to make up their deposit of 5% of the property price.

Impact of higher house prices and interest rates on today's first-time buyers compared to Q4 2005					
Region	Increase in typical first-time buyer house price 2005-2006	Increase in deposit required	Increase in borrowing required	Additional monthly payment assuming constant mortgage rate of 4.84%	Additional monthly mortgage payment assuming mortgage rate of 5.38%
Northern	11%	£517	£9,827	£57	£88
Yorks & Humber	11%	£562	£10,686	£61	£97
North West	8%	£416	£7,895	£45	£81
East Midlands	6%	£372	£7,074	£41	£77
West Midlands	7%	£396	£7,531	£43	£81
East Anglia	10%	£607	£11,539	£66	£108
Outer South East	9%	£639	£12,136	£70	£118
Outer Metropolitan	9%	£765	£14,537	£84	£139
Greater London	11%	£1,113	£21,145	£122	£191
South West	6%	£454	£8,618	£50	£95
Wales	10%	£555	£10,548	£61	£98
Scotland	18%	£776	£14,741	£85	£115
Northern Ireland	41%	£2,187	£41,556	£239	£285
<b>UK</b>	11%	£686	£13,041	£75	£118

Source: Nationwide Building Society.

Notes: Assuming repayment mortgage based on 95% LTV of typical first-time buyer property price of £128,105 in Q4 2005 and £141,832 in Q4 2006.

Assuming Nationwide homebuyer 2 year tracker rate of 4.84% in Dec 2005 and 5.38% today.

## Some of today's first-time buyers face a monthly mortgage payment of £285 more than they would have done this time last year

"Of course, much of this is due to the increase in house prices throughout the year. Keeping interest rates constant, during 2006 the increase in house prices alone would have added £75 to the monthly payment of a typical UK first-time-buyer, simply because of the extra borrowing needed to get on the housing ladder. However, the national picture, as always, hides the regional variations across the country. The deterioration in affordability resulting from faster house price growth alone was much more severe in some parts of the UK than others. Northern Ireland, where prices increased by a staggering 41% in 2006, stands out particularly. Here, a first-time buyer would have needed to find more than £2,000 extra for a deposit and borrowing costs would be almost £230 per month higher now than at the end of 2005 even without the rate rises. Taking the increase in rates into account, the total extra monthly payment increases to £285. First-time buyers in the East Midlands on the other hand, would have only had to find an extra £372 in deposit, but would still face £77 more per month in borrowing costs.

## Rate rises add over £50 to first-time buyer mortgage payments...

"Changes in interest rates have a separate effect on affordability, on top of the increase in house prices. In December 2005, before the rate rises, two-year tracker mortgages were available at 4.84%, a monthly mortgage payment of £700 on a typical first-time buyer homeloan of £121,700. After the Bank of England's moves, the rate increased by 0.75% to 5.59% bringing the monthly mortgage payment up by £54 to £754. Again, the differences in house prices mean that the impact of the rate rises are felt more acutely in some parts of the country than others. 2005 vintage first-time buyers on a tracker mortgage in Greater London for example, face an increase of £88 as a result of the rate changes, while those in Scotland and the Northern region of England face an increase of less than half this amount.

Impact of Rate Rises on First-Time Buyers Purchasing in Q4 2005							
Region	Typical first-time buyer house price Q4 2005	December 2005 (before rate rises)		February 2007 (after rate rises)		Monthly saving on fixed after rate rise	Total savings to date on fixed
		Monthly mortgage cost in December 2005 2 year fixed rate 4.89%	Monthly mortgage cost in December 2005 Tracker rate 4.84%	Monthly mortgage cost in February 2007 Tracker rate 5.59%	Increase in tracker mortgage payment		
Northern	£93,274	£512	£510	£549	£39	£37	£78
Yorks & Humber	£106,725	£586	£583	£628	£45	£42	£89
North West	£110,119	£605	£602	£648	£46	£43	£92
E Midlands	£114,649	£630	£627	£675	£48	£45	£95
W Midlands	£118,017	£648	£645	£695	£50	£46	£98
E Anglia	£127,138	£698	£695	£748	£53	£50	£106
Outer S East	£146,518	£805	£801	£862	£61	£57	£122
Outer Met	£168,707	£927	£922	£993	£71	£66	£141
Greater London	£209,894	£1,153	£1,147	£1,235	£88	£82	£175
S West	£143,095	£786	£782	£842	£60	£56	£119
Wales	£112,333	£617	£614	£661	£47	£44	£94
Scotland	£84,510	£464	£462	£497	£35	£33	£70
Northern Ireland	£107,874	£593	£590	£635	£45	£42	£90
<b>UK</b>	<b>£128,105</b>	<b>£704</b>	<b>£700</b>	<b>£754</b>	<b>£54</b>	<b>£50</b>	<b>£107</b>

Source: Nationwide.

Notes: Based on 95% LTV repayment mortgage. House price held constant for comparison

### ...except for those on fixed-rate deals

"Of course some borrowers will face no increase in their mortgage payment at all. While there was little to choose between the two-year tracker and two-year fixed rate mortgage costs at the end of 2005, developments since then have had a big impact.

"At the end of 2005 financial markets were expecting that the next movement in rates would be down. Taking out a tracker at the end of 2005 would have only cost about £4 less per month than a fixed rate loan, but if you believed the markets and expected a further 0.25% cut in rates, this would have increased the saving to £21 per month. As it turned out rates increased and taking out a fixed rate loan then would have saved around £107 in total to date and an extra £50 per month after the next rate rise takes effect. The biggest savings are in the most expensive areas of London and the South East where the overall amount of borrowing is higher.

### More first-time buyers take out longer-term and interest-only loans

"One way that borrowers can try to keep their monthly payments down is to increase the term of the loan. 25 years is the traditional length of the loan, but increasingly first-time buyers have been taking out longer-term mortgages. The majority of first-time buyers still take out a loan of between 21 and 25 years, but the proportion taking out a loan of 26 or more years increased from 28% in Q3 2005 up to 34% in Q3 2006. Extending the term of the loan can reduce monthly payments significantly. On average in the UK mortgage payments are reduced by £63, but in London this increases to £103. In spite of higher house prices, London has seen little change in the proportion of first-time buyers taking out longer-term mortgages and the overall proportion of Londoners taking out a loan of 26 years or more is only 19%. However, for those borrowers that do choose a longer-term, this comes at a high price. The total amount repayable on an average property over the full life of the loan would be more than £25,000 higher on a 30-year mortgage than on a 25-year homeloan.

Impact of longer mortgage term on first-time buyer affordability					
Region	Typical first-time buyer house price Q4 2006	Monthly cost over 25-year term	Monthly cost over 30-year term	Monthly saving	Total extra payment over life of mortgage
Northern	£103,618	£597	£552	£46	£19,313
Yorks & Humber	£117,973	£680	£628	£52	£21,988
North West	£118,430	£683	£630	£52	£22,073
East Midlands	£122,096	£704	£650	£54	£22,757
West Midlands	£125,944	£726	£670	£56	£23,474
East Anglia	£139,284	£803	£741	£62	£25,960
Outer South East	£159,293	£918	£848	£71	£29,690
Outer Met	£184,009	£1,061	£979	£82	£34,296
Greater London	£232,152	£1,339	£1,236	£103	£43,269
South West	£152,166	£877	£810	£67	£28,361
Wales	£123,436	£712	£657	£55	£23,006
Scotland	£100,027	£577	£532	£44	£18,643
Northern Ireland	£151,617	£874	£807	£67	£28,259
<b>UK</b>	<b>£141,832</b>	<b>£818</b>	<b>£755</b>	<b>£63</b>	<b>£26,435</b>

Source: Nationwide.

Notes: Based on 95% LTV repayment mortgage at current 2 year tracker rate of 5.38%

"Taking out an interest-only loan is another way to reduce monthly outgoings and first-time buyers have been doing more of this too, although it is not necessarily true that first-time buyers are systematically using interest-only loans for income stretch<sup>1</sup>. This time last year 20% took out interest-

<sup>1</sup> See Tatch, J (2006) *Interest-only: why all the interest?* CML Housing Finance

only loans, compared with 25% now. At current rates an interest-only loan on an average property would cut mortgage payments by £214. In London the saving would be around £350. But again a cheaper monthly payment now is not without strings. Not making early provision to repay the capital at the end of the mortgage term would be a highly risky and uncomfortable strategy.

<b>Impact of interest-only loan on first-time buyer affordability</b>				
Region	Typical first-time buyer house price Q4 2006	Monthly cost on 25-year repayment mortgage	Monthly cost on 25-year Interest-only mortgage	Monthly saving with interest-only mortgage
Northern	£103,618	£597	£441	£156
Yorks & Humber	£117,973	£680	£502	£178
North West	£118,430	£683	£504	£178
East Midlands	£122,096	£704	£520	£184
West Midlands	£125,944	£726	£536	£190
East Anglia	£139,284	£803	£593	£210
Outer South East	£159,293	£918	£678	£240
Outer Met	£184,009	£1,061	£784	£277
Greater London	£232,152	£1,339	£989	£350
South West	£152,166	£877	£648	£229
Wales	£123,436	£712	£526	£186
Scotland	£100,027	£577	£426	£151
Northern Ireland	£151,617	£874	£646	£228
<b>UK</b>	<b>£141,832</b>	<b>£818</b>	<b>£604</b>	<b>£214</b>

Source: Nationwide Building Society

Notes: Based on 95% LTV at current 2 year tracker rate of 5.38%

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