Orchid Financial Services Ltd

Getting on the property ladder

What steps do you need to take?

Buying your first home is one of life's milestones, but how easy it is to realise depends on your own circumstances and to a lesser extent where you live in the UK.

Most first-time buyers in England and Northern Ireland are able to get on the property ladder without paying stamp duty after Philip Hammond abolished the property tax on all transactions worth less than £300,000 in November 2017.

In many ways the chancellor blazed a trail for other politicians to follow, as his Welsh equivalent, finance secretary Mark Drakeford, raised the land transaction tax (LTT) threshold from £150,000 to £180,000 just three weeks later.

Not to be left behind, Scotland's finance secretary Derek Mackay proposed increasing the land and buildings transaction tax (LBTT) threshold to £175,000 for first-time-buyers – but this measure is yet to be confirmed.

Wherever you are in the UK, the same core principles apply. First you need to save, then you need to research where you want to buy your home and finally you need to secure a mortgage.

Saving your deposit

Stashing away a certain amount of your wages each month is a good habit to get into. Not only will it help you save for a deposit to buy your first home, it can help you save for a comfortable retirement.

Your deposit will be what helps you secure a mortgage, and in the current market you will need to save at least 5% of a property's value to gain a lender's approval.

For example, you would need to save a minimum of £7,500 if you want to buy a property worth £150,000. You would then need to borrow £142,500 from your mortgage provider.

The average first-time buyer in the UK has to save for eight years to achieve a deposit, although the typical amount of the deposit varies depending on where you want to buy your first home.

In London, where the saving period is usually longer, the typical buyer needs to save £80,000 to take their first steps on the property ladder, compared to £20,000 elsewhere in the UK.

If you're struggling to save for a deposit, you may consider other methods such as pooling resources to buy a home with trusted friends or getting financial help from your family.

The second approach is littered with various pitfalls and it is therefore imperative to seek expert advice before accepting such gifts.

ISAs

One popular savings method is the government's Help to Buy ISA, which allows you to save up to £200 a month towards buying a first home worth up to £250,000 (or £450,000 in London).

More than 320,000 first-time buyers have utilised the scheme, which offers a maximum government bonus of £3,000 on capped savings of £12,000.

Therefore, for someone who has made the maximum deposit (£1,000) and is putting away the £200 monthly limit, it would take four years and seven months to save the maximum £12,000.

These ISAs will be open for new applicants until 30 November 2019, while the government bonus is only added once the government is certain the transaction will go ahead.

The Lifetime ISA is a similar savings product with a similar bonus, but can be used for either retirement saving or for buying a home.

It's only available to under-40s, and it's possible to save up to £4,000 a year into a Lifetime ISA and receive the £1,000 government top-up.

A Lifetime ISA can be used for a first home or to supplement retirement income after the age of 60, and the government bonus is added annually up to the age of 50.

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However, if it's cashed in before the age of 60 and the money is not used to buy a first property or in the event of terminal illness, a 25% exit charge applies.

How do mortgages work?

Two of the most common mortgages on the market are repayment mortgages and interest-only mortgages.

Each monthly payment goes towards both the capital and the interest with repayment mortgages, while you pay just the monthly interest charged on the loan with an interest-only mortgage.

With interest-only mortgages, you don't have to repay what you've borrowed until the end of the term.

The bigger deposit you have, the less you will have to pay back – both in terms of your monthly repayments and over time.

Larger deposits are also considered by lenders to be less risky.

The cheapest mortgage deals on the market right now require at least a 40% deposit, although this is unrealistic for most first-time buyers who generally have a deposit of 17%.

Your lender has the power to repossess your home if you cannot maintain your monthly payments.

Securing your mortgage

If you have a suitable deposit and can afford the monthly repayments without being overstretched, you're probably in a good place to secure a mortgage to buy your first home.

However, getting a mortgage isn't as simple as saving a deposit. You also need to have a good credit score and pass an affordability assessment as lenders give serious consideration to these as well.

To get the most competitive mortgage deals you will usually need a deposit of more than 25%, while some of the best deals require 30% or even 40% deposits.

You also need to consider the economic climate, particularly the relationship between interest rates and inflation, when it comes to taking out your first mortgage.

Mortgage options

Deciding which type of mortgage to take out is a key decision, and it's important to understand how they work.

You'll pay an initial interest rate over a set period of time after taking out your mortgage.

This rate can be guaranteed not to change (fixed rate) or may increase or decrease (tracker), usually over two and five years.

A fixed-rate mortgage ensures your mortgage repayments remain the same until a fixed period of time ends, and are based on the interest rate at the time you take on the product.

These can be attractive when it looks like interest rates may be set to rise or if you want certainty about your payments, but lack appeal when interest rates look set to fall over a period of time.

Tracker mortgages are a type of variable rate mortgage, where the interest rate tracks the Bank of England base rate (currently 0.5%) at a set margin (such as 1% below or above it).

For example, with the current base rate of 0.5%, a +1% tracker mortgage would charge a rate of 1.5% interest – although this rate will change when the Bank of England changes the base rate.

It's imperative to seek professional advice to find out which mortgage type suits your circumstances.

Additional fees

Unless you're buying a first home worth more than £300,000 in England and Northern Ireland or £180,000 in Wales, you probably won't need to worry about paying whichever property tax applies.

As it stands, first-time buyers in Scotland will only pay land and buildings transaction tax on any residential purchase of more than £145,000, although this may be raised to £175,000 for first-time-buyers in the summer.

Above these thresholds, buyers will pay whichever property tax applies to them at the following rates in 2018/19:

England & Northern Ireland		Scotland		Wales	
£0 – £125,000	0%	£0 – £145,000*	0%	£0 – £180,000	0%
£125,001 – £250,000	2%	£145,001 – £250,000	2%	£180,001 – £250,000	3.5%
£250,001 – £925,000	5%	£250,001 – £325,000	5%	£250,001 – £400,000	5%
£925,001 – £1.5m	10%	£325,001 – £750,000	10%	£400,001 – £750,000	7.5%
Over £1.5m	12%	Over £750,000	12%	£750,000 – £1.5m	10%
				Over £1.5m	12%

*This may rise to £175,000 from June 2018 (subject to consultation).

In addition, there are various other fees you do need to budget for so make sure you add the full costs of buying a house and mortgaging before you get started.

You also need to consider mortgage fees, survey fees and legal fees. It's possible to minimise them, but you can't magic them away.

Contact us to discuss saving for your first home.