

Understanding Mortgage Affordability

As a mortgage broker, our role is pivotal in helping clients achieve their dream of homeownership. One critical aspect to obtaining a mortgage is **affordability**—the cornerstone of successful mortgage applications. In this blog, we'll delve into what you need to know about affordability, common challenges, key variables affecting it, and as a broker, how we can provide valuable assistance to you.

What Is Mortgage Affordability?

Mortgage affordability refers to the borrower's (you) ability to repay the loan they wish to take out. Lenders assess this carefully to prevent borrowers from overextending themselves financially. Here's how it works:

- 1. Income Assessment:** Lenders evaluate your income, including salary, bonuses, and other sources.
- 2. Debt Consideration:** Existing debts (credit cards, car finance, personal loans) impact affordability. High debt levels may limit borrowing capacity. All personal debt needs to be included.
- 3. Spending Habits:** Lenders analyse monthly expenses to gauge affordability realistically.

Challenges in Affordability

- 1. Rigorous Affordability Assessment:** Lenders are cautious due to the severe consequences of defaulting on a mortgage can have on borrowers.
- 2. Risk Comparison:** Falling behind on mortgage payments is riskier than missing rent. Lenders consider this when approving repayment schedules.

How Much Can Clients Borrow?

- Most applicants can borrow 4-4.5 times their annual income.
- Some lenders may offer up to 5 times the income. This will depend on several factors which a broker can advise further on.
- Example: If the income is £30,000, borrowing capacity ranges from £120,000 to £150,000.

What Is Stress Testing?

Stress testing is a crucial step in assessing mortgage affordability. It involves evaluating how borrowers would cope with adverse scenarios, such as:

- 1. Interest Rate Increases:** Imagine a sudden rise in interest rates. Would the borrower still afford their mortgage payments?

2. Income Reduction: What if the borrower's income decreased unexpectedly due to job loss or other factors?

3. Life Events: Consider life events like illness, family emergencies, or unexpected expenses.

Broker's Role in Stress Testing

As a broker, we play a vital role in stress testing:

1. Explain the importance of stress testing. Clients need to understand potential risks.
2. Run scenarios with clients. Calculate affordability under adverse conditions.
3. Suggest building a financial buffer to handle unexpected situations.

Stress testing ensures responsible lending and protects both borrowers and lenders.

How Brokers Assist in Understanding Affordability

1. Expert Guidance: Brokers understand the intricacies of affordability calculations. They guide clients on optimising their financial situation.

2. Lender Comparison: Brokers compare multiple lenders, finding the best fit for each borrower's unique circumstances.

3. Negotiation Skills: Brokers negotiate to work with lenders to deliver, if possible, favourable outcomes for borrowers.

4. Paperwork Management: Brokers handle paperwork, streamlining the process for borrowers.

Conclusion

By collaborating with a skilled mortgage broker, borrowers gain a strategic advantage and can be the difference between meeting lenders' affordability criteria, or not!

Give Derwent Mortgages a call if you would like to know more.