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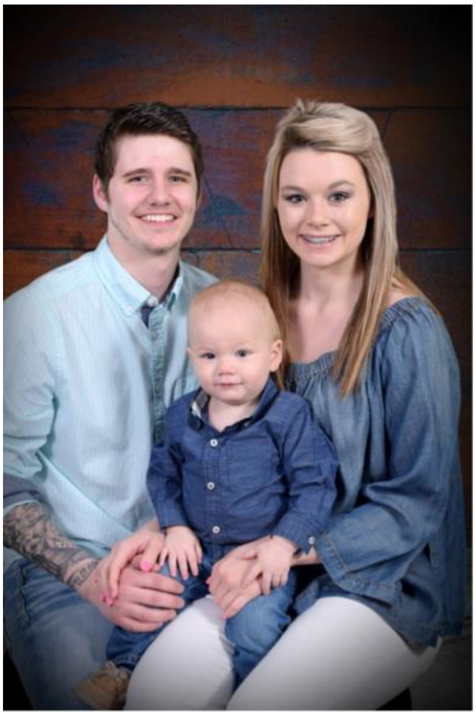
Lancaster Royal Grammar School

PFP Erasmus+
Module 5: Mortgages

Mortgages case study



The Wilsons are a young family from Lancashire and they have a four year old child. They have recently decided they want to own their first home as a family so are looking into what kind of mortgage would suit them best. Mr Wilson has been a postman for 6 years and is 25 years old and is earning a yearly income of £17,970. They have been living with his parents until now so have been able to save up a £25,000 deposit for a new home. Mrs Wilson (24 years old) has recently qualified as a nurse and is earning £23,465 a year, she currently works for the NHS but is considering moving into private healthcare so she could increase her income. As she went to university she doesn't have any savings and also has some student debt. The advantage of working for the NHS as a nurse is that it provided good job security.
The apartment they are looking at is a 2 bed first floor on a cul-de-sac, its current sale price is £81,950 (stamp duty exempt) and they see themselves living there for around 4 or 5 years as they hope to move into a bigger property in the future. Neither Mr nor Mrs Wilson have any problems with their financial history as only Mrs Wilson has ever used an overdraft and that was for a very short amount of time and for a small amount. Neither of them want to take risks when it comes to money as they both want to be sure of how much disposable income they have to spend. Most mortgage deals they are reviewing allow for an average of 4 times combined earnings.

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Questions

Q1: Analyse which type of mortgage would best suit the Wilson family?

Q2: Calculate the current deposit percentage the Wilson's can use?

Q3: What advice could you offer the Wilson's to reduce their financial risks when buying the new property?

Q4: If the Wilson's decreased their deposit, what effect would this have on the potential range and costs of mortgages available to them?

Q5: What strategies could be employed to reduce the total mortgage debt payable?

Q6: What is stamp duty?

Q7: Calculate the typical maximum mortgage that the Wilson's could borrow?

Q8: What level of deposit would the Wilson's need to save to secure the best mortgage deals when purchasing the apartment?

Q9: Before the Wilson's purchase the apartment, what other factors and issues should they consider?

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Answers

Q1: Analyse which type of mortgage would best suit the Wilson family?

Given the Wilson's cautious attitude to risk they be best suited to a fixed rate mortgage of 2year or 5 years duration.
This would mean they would find budgeting easier and be able to estimate their disposable income
A fixed rate mortgage may not be the best option if interest rates fall but it would mean they are protected from interest rate rises
Fixed rate mortgages can have high set up and redemption costs.
If the Wilson's only fix the mortgage rate for 2 years they would then go onto the lending SVR or they could get another mortgage deals but this would involve set up fees.

Q2: Calculate the current deposit percentage the Wilson's have available for the potential apartment purchase?

£25,000/£81,950 x 100 = 30.5% deposit

Q3: What advice could you offer the Wilson's to reduce their financial risks when buying the new property?

Consider a fixed rate mortgage deal. Ideally with a longer fixed period.
Consider purchasing mortgage protection/income protection insurance
Perhaps Mrs Wilson should stay with the NHS as it has reasonable job security compared to the private sector

Q4: If the Wilson's decreased their deposit, what effect would this have on the potential range and costs of mortgages available to them?

The bigger the deposit means the lower the LTV (loan to value) of the mortgage. If the Wilson's reduced their deposit they would have fewer mortgages available to them and the interest rate on the loan would be likely to increase

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Q5: What strategies could be employed to reduce the total mortgage debt payable?

The Wilson's could overpay their monthly mortgage and/or reduce the length of the mortgage. They could also look to secure the best interest rate they can

Q6: What is stamp duty?

A tiered tax on property purchases. Currently 1st time buyers are exempt up to a property value of £300,000

Q7: Calculate the typical maximum mortgage that the Wilson's could borrow?

Combined income: £17,970 + £23,465 = £41,435 x 4 (typical income multiple) = £165,740

Q8: What level of deposit would the Wilson's need to save to secure the best mortgage deals when purchasing the apartment?

£81,950 x 0.4 = £32,780 (this is 40% of the purchase price)

Q9: Before the Wilson's purchase the apartment, what other factors and issues should they consider?

Affordability, the official valuation of the apartment, the structural survey of the apartment, what is predicted to happen to house prices and the economy, is the apartment leasehold, what is the annual maintenance charge and ground rent for the apartment

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