

This guide looks at interest-only mortgages and:

- Looks at the risks
- Suggests repayment strategies

**A growing problem:** According to the Council of Mortgage Lenders, 61,000 first-time buyers (and more than 200,000 homebuyers altogether) arranged an interest-only loan in 2005 without *any* repayment vehicle in place). More than one in seven first-time buyers now take out interest-only mortgages.

Interest only mortgages appear (because you don't pay off your debt until the end of the mortgage term) much less costly than repayment mortgages. For example, a £100,000 interest-only loan with an annual interest rate of 5% costs £416.67 a month, roughly £2000 pa. less than its repayment equivalent. Of course, with the interest-only option you are still going to have to find the dosh to repay the principal at some point.

But, an interest-only home loan that isn't backed by a plan to repay the amount you borrowed, as well as the interest is high-risk, because it relies on you making your own arrangements to repay the mortgage principal when the time comes.

**Staying safe:** So, How do you ensure an interest-only mortgage does not become a financial millstone:

**Make the mortgage longer:** By choosing the longest possible mortgage term you could reduce the monthly repayments you need to go the more secure repayment route. For example, a £100,000, 25-year, 5% repayment mortgage costs £585 a month. Over 35 years this becomes only (!) £505 a month.

**Use “interest only” just to get you started:** Interest only is, granted, the only way some can afford to get on the property ladder. But, If you are in the early years of a profession where earnings are likely to rise much, much higher in the future (maybe you are a trainee accountant, doctor, solicitor or barrister – or plumber?), you could opt for an interest-only mortgage now and then switch to a repayment mortgage once your income has risen.

**Change when you move:** Go for a repayment mortgage when you make

your next house move. Don't do this if you are in your late forties or beyond.

**Set up a monthly savings plan:** If you can set aside money for a long period (at least ten years), you have a very good chance of getting more back from an investment in shares, rather than cash savings. Think about opening a share ISA and making monthly contributions to a low-cost investment such as an index-tracking fund. Or, start or increase your contributions to a pension and later withdraw a tax-free lump sum to pay off your mortgage.

**Go 50/50:** If you can't afford a £100,000 repayment loan, why not look into a £50,000 repayment loan and a £50,000 interest-only loan?

**Pay more than you need, whenever you can:** You could help pay off your mortgage, making regular or lump sum overpayments. This works best with flexible, offset or current account mortgages, where you won't be penalised for cutting into your debt as and when you can.

**Trade down:** If the worst comes to the worse, you can sell your home, pay off your loan, and use the remaining cash to buy somewhere less costly. We don't think that will be a very attractive prospect for many – but it could be what some are forced to do.

**Whatever you do, don't cross your fingers and hope for the best:  
Relaying on the lottery to pay of your mortgage is not an option (well,  
only a 14 million to one option!)**