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Digging Deeper

Residential Analysts Ltd

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Mortgage Repayments

As mortgage rates rise, attention is inevitably focussed on what impact they will have on borrowers' mortgage repayment affordability. However, there is a lack of public data on borrowers' actual repayments and many of the available data sources are constrained by the assumptions contained within. This note provides a quick summary on some of these sources and suggests that repayment affordability is better than some of them show.

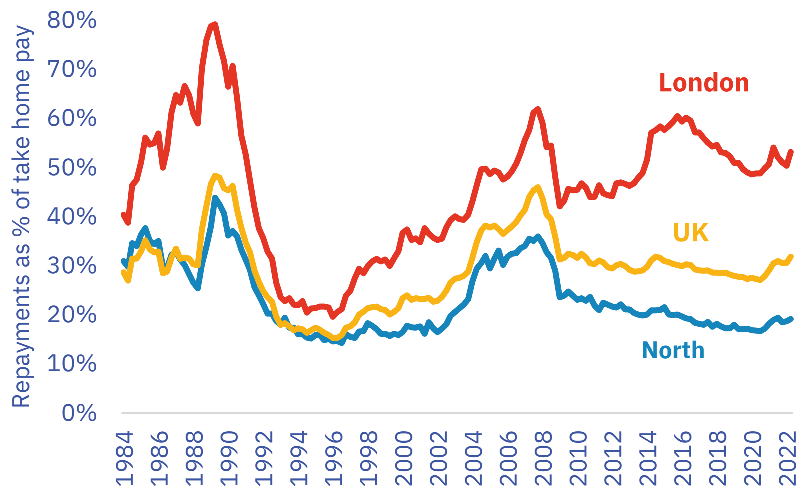
Looking Beyond The Assumptions

One of the most popular data sources, given its timeliness and accessibility is the Nationwide series on first time buyer (FTB) mortgage repayments as a percentage of take home pay (Fig 1). One of the most striking features of the data is the very high repayments in London suggesting first time buyers are massively stretching themselves to buy a home in the capital.

However, this reflects the assumptions in the series rather than the reality of new borrowers. The data is based on ONS average earnings and not Nationwide's own borrowers – the average first time buyer now has a much higher income than the average wage and many borrow on the basis of a joint not single income.

Fig 1: FTB Mortgage Repayments

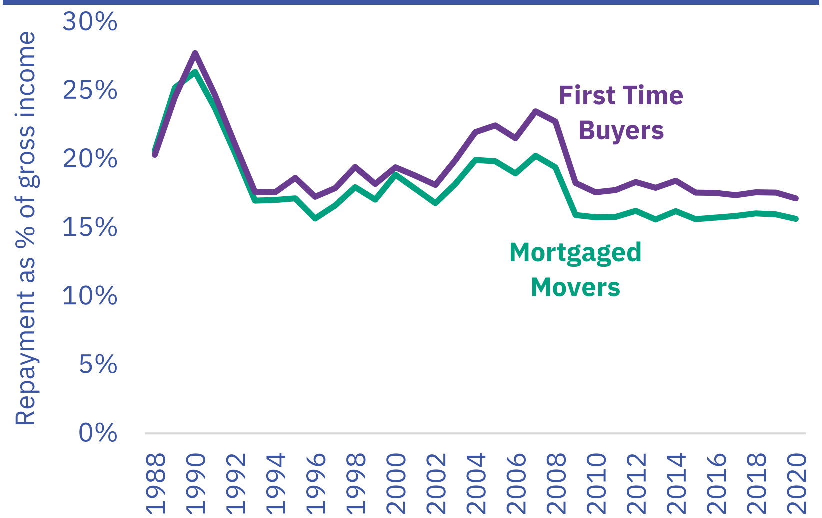
Source: Nationwide



The Nationwide series also assumes an 80% loan-to-value ratio (LTV). This assumption partly explains the apparently very high repayments during the late 1980s – a period when the availability of very high LTV mortgages (including above 100%) was at its highest and so the actual average was much higher than 80%. More recently, the average LTV in London is actually the lowest of any region given its very high price to income ratios (69% in 2021 according to calculations using ONS/RMS data). Therefore London first time buyers have been borrowing less than the Nationwide series assumes (while relying on more help with the deposit from their families). The series also assumes a 25 year mortgage term. This assumption is sensible for the entire period leading up to the financial crisis but the last decade has seen average terms extend – especially in more expensive markets. A final point is that while the series is based on take home pay, this only involves assumptions on tax and NI and not other factors such as student loan repayments and pensions. In summary, the Nationwide series tells us a lot about the housing market but only if we look past its misleading headline repayment figures.

Fig 2: Mortgage Repayments - UK

Source: ONS & Regulated Mortgage Survey



The ONS also publish data on repayment affordability based on a sample from the Regulated Mortgage Survey. However, it is only national and published annually - 2021 data is due later this month. It has the benefit of being based on the actual incomes of borrowers though it does use an average rather than actual mortgage rate so may not be a true reflection of affordability. However, its figures more closely correspond with DLUHC's English Housing Survey which shows mortgaged homeowners housing costs averaged around 18% of gross household income in 2020/21. Meanwhile, our own calculations (e.g. chart here) also show mortgage repayment affordability has been near record lows in recent years – the cost of buying rather than cost of owning has been the biggest barrier to homeownership. But that may now change as rates rise.