BALANCE
a commercial view

A NEW ERA FOR PROPERTY INVESTORS

As you may or may not be aware, the 30th September 2017 brought further change for the buy-to-let / property investment market and how lending institutions review funding applications from professional investors and landlords.

At the start of 2017, banks embedded the first of the PRA's changes to underwriting standards, which were designed to bring consistency to the lending landscape. Specifically with regard to minimum affordability requirements and what stress testing should be applied for different clients paying varying levels of tax within the transaction. This was with a view to protecting the investor community by ensuring they were only provided with sensible levels of debt that would be open to future refinancing.

The next evolution to the underwriting standards comes into force and asks lenders to ensure they have a full picture of the customer, and a complete understanding of their position with regard to their investment portfolio: *"The PRA expects firms undertaking buy-to-let lending to have regard to its potential business characteristics. The PRA considers that borrowers with four* **or** *more distinct mortgaged buy-to-let properties, either together or separately, in aggregate, should be treated as 'portfolio landlords'."**

*Prudential Regulation Authority (PRA)

Fortunately, these changes will have a limited impact on how Balance for Business transacts as many commercial lenders business models have always been based on underwriting each deal on its own merits. However we are all too aware of the impact this will have on the market as a whole, and the responsibility lenders have to support this transition. The lending community must rapidly communicate how this applies to their offering, and also how they plan to support their existing and prospective customers throughout this transition.

Balance for Business is pleased to offer some simple guidelines below:

FROM THE 1ST OCTOBER 2017, CUSTOMERS WILL BE CLASSIFIED INTO TWO BUCKETS

1-3 MORTGAGED PROPERTIES

This relates to **any** property/properties owned and mortgaged for **all** customers, and also includes the property intended for purchase/refinance at that time. Please note that if an investor is buying via a limited company but owns 3 properties in their personal name, they will cascade into the next bucket categorised as "Portfolio landlords" (please see below).

Please also note that the level of shareholding within that property is irrelevant – if they are a shareholder and the property is mortgaged, that property will count as one of the 3 allowed in this category.

Usually, cases that sit within this classification are considered relatively straightforward and can be submitted online, often obtaining an instant decision. The system will check personal credit position and that the property generates the necessary income to support the loan. These online systems are highly efficient and provide a quick service. This keeps lenders' costs down and may ultimately be passed through to the cost of the mortgage.

4 OR MORE MORTGAGED PROPERTIES (PORTFOLIO LANDLORD)

Where the customer is looking to buy or refinance their 4th mortgaged investment property, they will now be classed as a portfolio landlord. This means that the underwriting process required by the lender will look considerably different in terms of its complexity.

As with all regulation, the regulator does not dictate exactly what needs to be assessed and merely provides guidelines that lending institutions must interpret to ensure they demonstrate best practice and deliver a good outcome for the customer.

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THE LIKELY ELEMENTS THAT LENDERS WILL NOW CONSIDER ARE AS FOLLOWS

(PLEASE NOTE THIS IS NOT AN EXHAUSTIVE LIST)

• Many lenders will now require a business plan and cashflow forecast for all property businesses

• A review of the customer's full portfolio; does the customer have any geographical concentration risks within their portfolio? Lenders will need to ensure that they understand any risks and what the customer has in place to balance these risks

• What spread of products does the customer have? For instance, is there a significant portion of the overall debt on fixed rates that are due to expire, and do these deals still work bearing in mind today's mortgage prices? Lenders will look at rental income for these properties versus the debt outstanding, and check that it performs against current affordability calculations

• How highly geared is the portfolio? How much are the properties worth and what debt has been secured against them? As above, lenders must look at the customer's ability to refinance this debt in the future and whether the numbers work on today's affordability requirements

TO CALCULATE GEARING PERCENTAGE:

$$\frac{\text{MORTGAGES ON ALL PROPERTIES}}{\text{TOTAL CURRENT MARKET VALUE OF ALL PROPERTIES}} \text{ X100}$$

• What is the customer's personal income position? Do they live off this rental income alone and is this sustainable with rising investment costs? The lender will also consider how that customer manages any rental voids within the total income figure, and how this is balanced against the income needed to maintain their desired lifestyle

• Can the customer's returns model cope with the rising tax costs across their portfolio?

• The lender may also choose to sense check that the customer's tax code correctly reflects the affordability calculation

• Is there an effective long term plan or strategy in place for the customer's property business?

• The lender will also wish to review a picture of the customer's assets and liabilities to ensure that refinancing a property or adding another property to their portfolio will not cause any future issues

• Lenders must also evidence that they have reviewed the customer's overall cash flow to evidence that the customer can administer the management and maintenance of all costs across the portfolio

POTENTIAL MARKET IMPACT

• A review of the customer's full portfolio; does the customer have any geographical concentration risks within their portfolio? Lenders will need to ensure that they understand any risks and what the customer has in place to balance these risks

• What spread of products does the customer have? For instance, is there a significant portion of the overall debt on fixed rates that are due to expire, and do these deals still work bearing in mind today's mortgage prices? Lenders will look at rental income for these properties versus the debt outstanding, and check that it performs against current affordability calculations

• How highly geared is the portfolio? How much are the properties worth and what debt has been secured against them? As above, lenders will look at the customer's ability to refinance this debt in the future and whether the numbers work on today's affordability requirements

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POTENTIAL MARKET IMPACT (Continued)

Balance for Business is proud to have the right balance between technology and people, recognising the value to our customers in each of these areas. However those lenders reliant on a pure technological journey will need to add a manual underwrite into their current online process, and it is therefore likely that information will be required prior to getting indicative approval.

Some lenders may keep the initial assessment online, but you will need to be sensitive to money spent on a valuation where the deal has not been manually underwritten – especially where that lender's criteria has recently been amended.

Balance for Business has always taken a manual, case-by-case approach to assessing underwriting across all our Commercial Mortgages products, with dedicated and fully mandated teams "eyeballing" every deal to provide an assessment based on the merit of that case rather than on a credit scorecard, "computer says yes/no" approach. Alongside this we utilise lenders' technology to streamline processes in order to deliver the strongest service we can.

A huge benefit of this approach is that the changes outlined in this document do not have the same level of impact commercial brokers as they might for mortgage brokers. If anything, the changes actually mean our panel of lenders, underwriting in the 1-3 property range, will actually be less complex which we have reflected across the product range in terms of process.

However, it is important to note that we may see some institutions pulling out of the portfolio landlord market altogether and focusing purely on the "simpler" customers with 1-3 mortgaged properties. This highlights the need to build strong relationships with specialist commercial lenders like Balance for Business. We will continue to support the professional landlord and investor community with our experienced teams assessing each case on its own merits. Our aim is to support this market and help customers build and execute a long term and sustainable investment strategy.

In addition to other specialist advice services such as tax, we would thoroughly recommend that customers consult with their broker following these changes as they will be best positioned to advise on the wide range of individual circumstances that must be considered.

Call Us

One of our friendly advisors will be delighted to assist.

01752 227 966

Email Us

advice@balanceforbusiness.co.uk

PRA CHANGES
30TH SEPTEMBER 2017

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BROKER INFORMATION SHEET

NON-PORTFOLIO LANDLORDS

Improved criteria & process

As you may or may not be aware, the 30th September 2017 brought further changes for the buy-to-let market and how lending institutions review funding applications from professional investors and landlords.

KEY CRITERIA

When considering an application for a client that has no more than three mortgaged buy-to-let properties, the following is required:

BORROWER

• Borrowers must demonstrate experience of managing an investment property in line with our standard experience criteria for each product

• Borrowers must evidence - Payslips/SA302 or personal bank statements - to validate sufficient income to support personal living expenses

• No portfolio sheet required

SECURITY

• The property must yield sufficient income to support the monthly payment using the standard Balance for Business DSCR and stress test

• Please note that when considering outside income to support the rental (MAX 50% LTV), you will be required to complete a full income and expenditure assessment including evidence of income

PORTFOLIO LANDLORDS

No changes to our current criteria & process

"Borrowers that have four or more mortgaged buy-to-let properties (jointly or separately owned) either with Balance for Business or other borrowing entities".

KEY CRITERIA

When considering an application for a client that has more than three mortgaged buy-to-let properties, the following is required:

BORROWER

• Must demonstrate experience of managing an investment property in line with the standard Balance for Business experience criteria for each product

• Must evidence with either payslips or personal bank statements that they have sufficient levels of income to support personal living expenses

• We require a fully completed portfolio sheet to be submitted as standard

• Bank statements are required to evidence rental payments and mortgage histories (where not shown on CIAS)

SECURITY

• The property must yield sufficient income to support the monthly payment using the standard Balance for Business DSCR and stress test

N.B. Portfolio sheets for Commercial and STL cases will still be required.

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