

Interest Only Mortgage

Hello and welcome to this short presentation from Market Harborough Building Society - the mortgage world can be very daunting so we are here to help you through the maze of jargon.

Today we are going to discuss interest only mortgages.

When Market Harborough Building Society lends money it charges interest on the amount borrowed. An interest only mortgage means that each month you pay the interest charged by the Society but not the 'capital' or repayment of the loan itself.

Let us look at an example. You decide to borrow £100,000 for 25 years and the Society charges £500 a month in interest. Your mortgage payment would be £500. As you can see the balance you owe would remain £100,000 even at the end of the 25 year term providing you pay the monthly repayment.

So how do you repay the amount borrowed – the £100,000 I have just mentioned? As well as making a monthly payment to the Society you make an additional payment each month into a form of savings. Examples could be an ISA, a pension or as many have done in the past an endowment policy. The amount you save each month will grow and grow over the years until the end of the mortgage term. Remember you still owe the £100,000 borrowed originally as you have only paid the interest each month. When the mortgage term ends your savings should have grown to be at least the amount of the original loan: £100,000. You use the £100,000 savings to repay the mortgage in one big lump sum.

In recent years some people have taken interest only mortgages and whilst they have paid the lender the monthly interest they have not saved into a separate savings plan. This means you pay less per month than if you were saving as well as paying your interest only mortgage, and many people have taken an interest only mortgage to keep costs down. But it also means that you will never repay the mortgage unless something else happens. You may come into a windfall or inheritance to repay the sum borrowed. Or you may be looking to sell the property soon when the mortgage would be repaid. Some people look to use bonus payments from work to gradually repay the amount borrowed. However all of these options need very careful consideration before deciding if an interest only mortgage is right for you.

The other type of mortgage is a capital and interest mortgage or as it is sometimes known a repayment mortgage. As it suggests you repay the interest each month but at the same time you also pay back a little of the amount borrowed or capital as it is called. As time goes by the amount you owe gradually reduces as you make your regular monthly repayment until it reaches zero at the end of the mortgage term.

So in conclusion an interest only mortgage means the debt never reduces until the end of the mortgage term when the savings you have been paying into for many years should

have grown sufficiently to pay off the amount borrowed. However it is essential that you keep track of the savings to ensure they are on track to pay off the mortgage. This means they must also be available at the time you want the mortgage to end. If you don't save separately the mortgage will not be repaid and you will have to find the full mortgage balance at the end of the mortgage.

Thank you for listening. I hope it has been useful. Please give us a call on 01858 412250 and ask to speak to one of our friendly representatives if you wish to discuss your mortgage needs further.