First Time Buyers
The Bank of Mum and Dad

AUGUST 2018

Introduction

Overview of the UK Housing Market

Over the past 20 years, the average house price in the UK has risen from just under £70,000 in 1998 to £227,000 in 2018

For many first time buyers, the UK housing market looks particularly bleak. Constant increases in house prices up and down the country, combined with slow - almost stagnant - wage growth has led many to see home ownership as little more than a distant, unattainable pipe dream.

Over the past 20 years, the average house price in the UK has risen from just under **£70,000 in 1998 to £227,000 in 2018** — a statistic that jumps to a **370% increase** of £103,000 to £485,000 over the same period in London. A rapid rise in house prices has also seen an equally rapid rise in the size of deposits. In 2018, first time buyers looking to acquire a mortgage will have to fork out a 10% deposit of almost £50,000 in London - or only £16,500 in Northern Ireland.

While these house prices and mortgage deposits have been growing rapidly, the growth in wages has certainly not kept up. In fact, a **recent ONS report** demonstrated that, in 1997, the average house cost 3.5 times the average yearly salary, now the price of the average home is 7.8 times the average salary. Despite this, there are plenty of schemes out there designed to help first time buyers get onto the housing ladder. Schemes introduced by the UK government such as 'Help to Buy', LISAs (lifetime individual savings accounts) and first time buyer mortgages are all available and offer welcome encouragement for those looking to climb the property ladder.

Even with these schemes, first time buyers may still feel that it's almost impossible to get a foot on the ladder. Despite the somewhat worrying and undoubtedly unpromising statistics above, the number of first time buyers actually reached a nine-year high in 2017, with a **75% increase in people buying their first home** since the recession in 2009. There are also fewer second properties being purchased by private landlords - due, in part to the additional 3% stamp duty that new landlords have to pay - and the phasing out of the ability for landlords to deduct mortgage interest against rental income. These former rental properties are often ideal for first time buyers, meaning that 2017 also saw the most first time buyer properties available in the past decade.

The Bank of Mum and Dad is an incredibly important force in both the housing market and more general finance markets.

Introduction

Bank of Mum and Dad

This growth in first time buyers (FTBs) is not just helped by the aforementioned schemes. In fact, the 'Bank of Mum and Dad' is a major factor when it comes to getting FTBs on the housing ladder. **Nearly two thirds (62%)** of all homeowners under 35 received financial help from family or friends. In fact, more than £6.5 billion was lent by the Bank of Mum and Dad in 2017 - putting it on par with **the UK's 9th largest mortgage lender.**

The average contribution from parents to a first time buyer child **will likely be £18,000 this year**; that's a very substantial amount, but it's actually a drop of 17% from the 2017 average of £21,600. Although this drops to a low of around £11,000 in Scotland and jumps to a high of £31,000 in London.

The bank of mum and dad (BOMAD) isn't just for first time buyers, although it may indeed feel that way. That's right, it's not only FTBs who are borrowing from the BOMAD; **in fact 26% of current homeowners** said that they would expect financial help from family and friends. Furthermore, **58% of people who already own a home** and are considering a move said that they couldn't afford it without financial support from the BOMAD.

It's clear then, that the Bank of Mum and Dad is an incredibly important force in both the housing market and more general finance markets. In this white paper we'll be examining the ways that parents can help, the specifics regarding how money can and should be given to children, and the effect that the Bank of Mum and Dad is having on the economy.

How parents can help

Unfortunately, providing financial assistance to help your children become a first time buyer is not as straightforward as you may think. Rather than simply paying money into their bank account or offering them a straightforward loan, there are a number of hoops you may have to jump through before reaching the money lending or gifting stage. To start with, you will have to decide which aspect of the home buying process you would like to assist with.

A brief overview of the avenues parents can take to offer financial assistance:

Guarantor mortgages:

Rather than actually joining in with the purchase of a property, this type of mortgage will have you guaranteeing that you will cover any missed mortgage payments. Lenders are likely to see first time buyers pursuing this route as more creditworthy.

Learn more

Helping with a mortgage deposit:

Likely the most popular route that the BOMAD provides assistance with. This simply involves gifting or lending money to your children to help them put down a mortgage deposit on a home.

Learn more

Offset mortgages:

These mortgages allow you to offset the cost of your child's mortgage with your own savings. This allows your savings to be used as a deposit, while also lowering interest rates. For many offset mortgages, the savings can be used anytime, but reduces the benefit of the offset account. For certain specific offset mortgages such as the Barclays Springboard, savings funds are required to be kept in the offset account for a minimum period.

Learn more

Joint mortgages:

Choosing to help out with a joint mortgage will see you actually taking out a mortgage alongside your child. This can be beneficial as a lender will likely view you as more creditworthy. In addition, the parents may not have to be registered on the title deeds, avoiding the potential 3% additional stamp duty for a second property.

Learn more

Equity release:

Equity release is an option increasingly growing in popularity. It allows parents over 60 to release part of the equity in their homes to provide their children with a deposit as a gift. This allows parents to give money to their children while they are alive and see the benefits of their gift, rather than having to wait until they can leave them an inheritance when they die.

Learn more

Helping with a mortgage deposit

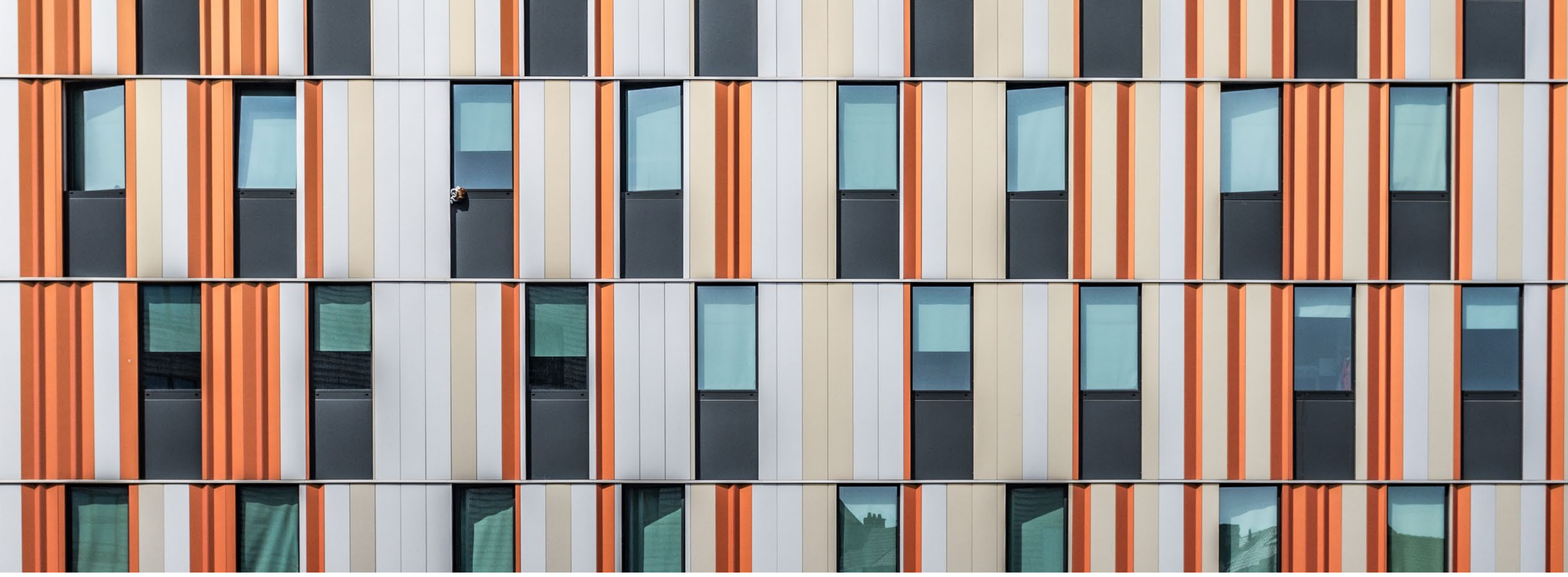
For many parents, the primary method through which they intend to help their children get on the property ladder is by simply giving or lending them money to be put towards a deposit. This is a very straightforward way for you to contribute from the bank of mum and dad. Parents get to choose an exact amount of cash to provide, while setting your own restrictions on how it is used. Despite the ease of this, it may not always be the best option if the parents don't have large amounts of money at their disposal.

Parents should check the inheritance tax implications of a gift when considering this option. Gifting a deposit may be a very beneficial option depending on the amount given and the IHT implications facing the parents.

Of course, this situation will only work for parents who have the money to gift, and who have a great deal of trust in their children.

Even parents with enough money to gift as a house deposit may not wish to simply give money to their children unchecked. In these situations, the money may not be used exactly as the parents see fit. Parents feeling as though they may face this scenario could consider loaning the money, but this could be unacceptable to some lenders who will only accept a loaned deposit if the payments on the loan agreed between parent and child are deemed affordable alongside the mortgage.

If parents don't have the capital at hand to provide a loan or gift to their children, we have outlined alternative ways through which the Bank of Mum and Dad can help first time buyers in the following pages.



Joint mortgage

With a joint mortgage, the cost of a mortgage is shared between a number of parties who will all be considered owners. Each owner is listed on the property deeds and everyone involved is collectively responsible for the mortgage repayments.

Both parents and children are responsible for the total cost of the mortgage

A joint mortgage can be very beneficial as an avenue through which the BOMAD can provide for first time buyers. Both parents and children are responsible for the total cost of the mortgage so must decide on a method of splitting payments between them. Plus, thanks to what is likely a longer and stronger credit history, lenders are likely to be more willing to lend greater amounts to those undertaking a joint mortgage with their parents.

Despite this, a joint mortgage is not perfect and there are a number of drawbacks to setting one up between parents and children. The parents must be able to view the child or children they are sharing a mortgage with as mature, financially independent adults who you can treat equally when making financial decisions about a property. Furthermore, the age of the parents may reduce the available mortgage term and increase the monthly payments. Aside from the added financial responsibility involved in acquiring a joint mortgage with your children, a joint mortgage could be off-putting due to the extra stamp duty involved if the parents already own a home - though this can be avoided if the parents choose to pay the mortgage without being registered on the property deeds. It's also worth being aware that, the parents own credit rating and ability to borrow will also be affected by being party to a joint mortgage.

If you are a very financially stable parent willing to view your children as financial equals, a joint mortgage could be ideal. Otherwise, it may be best to seek out another way to make use of the bank of mum and dad.

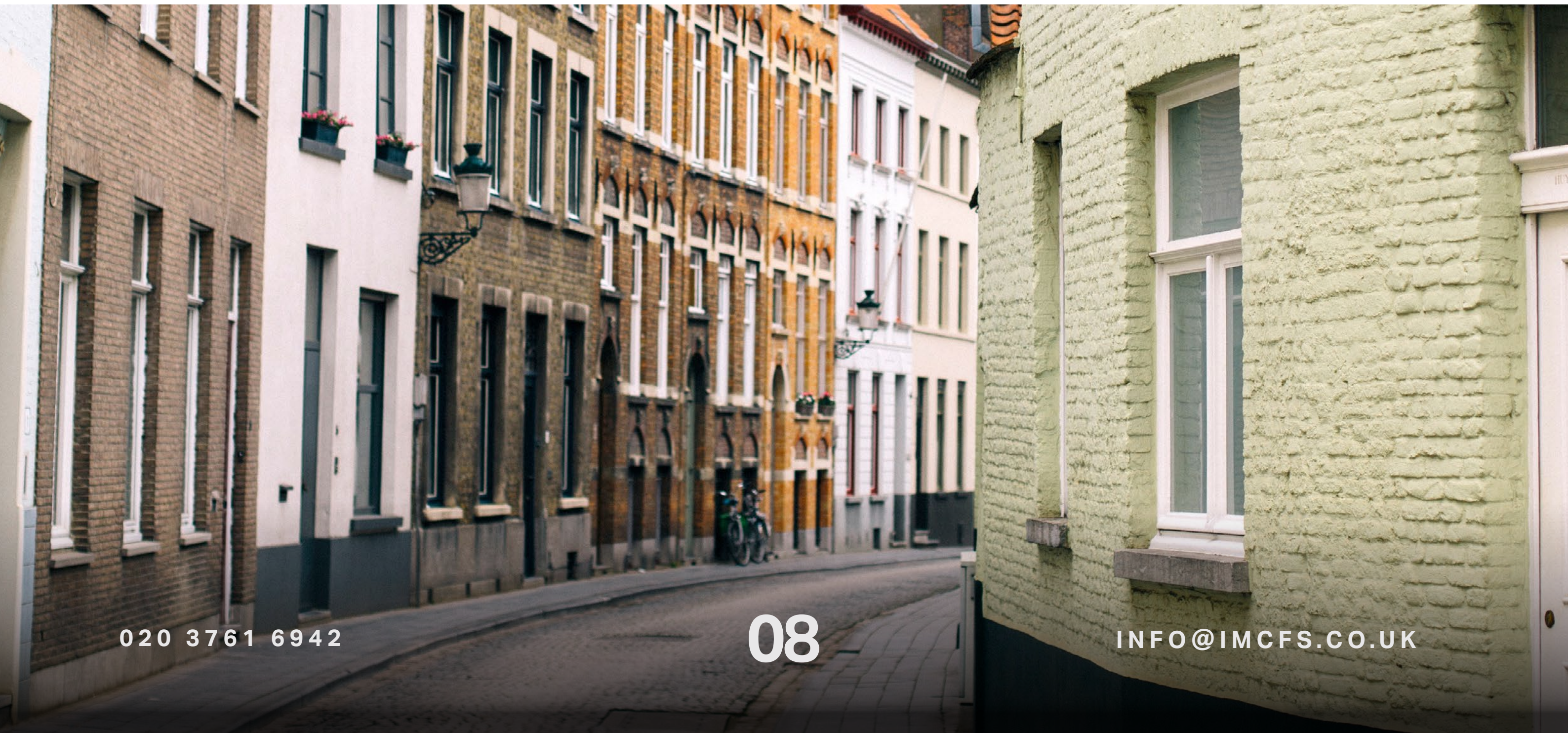
Guarantor mortgage

Often referred to as a ‘family’ mortgage, guarantor mortgages are a viable option for first time buyers receiving help from their parents. Unlike a joint mortgage, the parents have no responsibility to pay the mortgage alongside their children. Instead, they guarantee that they will cover their child’s mortgage if the payments are not made on time.

A guarantor mortgage is perfect in a situation where a mortgage would otherwise be unattainable due to lack of funds or a weak financial situation. To be a guarantor, parents will need to own their own property and prove that they have a high enough income to cover any payments that may need to be made on behalf of their child. Of course, they’ll also need to have a high enough credit rating for the lender to believe that they would be able to cover any missed payments.

One downside of such a mortgage is that the age of the guarantor could prevent any long term mortgages from being offered. However, as long as the guarantor’s income at the point of application and over the term of the mortgage will be sustainable, they shouldn’t face any issues.
Of course, if the mortgage goes unpaid, the guarantors will have to make up the cost - which could see them having to remortgage their home. In a worst case scenario, the parents’ home may be subject to repossession if their children default on their mortgage.

Despite the benefits of guarantor mortgages, they are falling in popularity. Instead, joint mortgages with parents not on the property deeds may be seen as a more viable, more modern alternative.



Offset mortgage

A family offset mortgage - often seen in the form of the **Barclays Family Springboard Mortgage** - allows parents or grandparents to link their savings to the child's mortgage. It can be seen as a way to give money to a first time buyer, without giving them direct access to the cash. These savings effectively become an additional deposit that lowers the overall cost of the mortgage.

As an example, a 2.5% mortgage of £100,000 could be offset by £10,000 of family savings. Now, the child is only paying interest on £90,000, saving £250 per year. Due to the lower amount that the child needs to pay back, the term of the mortgage can be shortened while making the same monthly payments as before, or the term can remain the same while the monthly payments are less.

Like any option, offset mortgages are not suitable for everyone. Higher rates come as standard for these mortgages, so you'll have to ensure that you have enough savings to make paying a higher rate worth it. A good benchmark to avoid feeling shortchanged by the higher rates of this kind of mortgage is to only consider offsetting if you have savings that make up 20% of the mortgage. Even then, it's still best to seek impartial financial advice before committing to an offset mortgage.

Equity release

The IMC team have laid out the ways in which equity release works - as well as its pros and cons - in a **previous article**. In that article, we looked into the ways in which equity release can benefit retirees by providing an additional boost to a pension. However, equity release could also be an ideal solution for parents looking for extra money to give to their children.

Equity release **has exploded in recent years**, with many older people releasing the money tied up in their homes, allowing it to be used today. Any equity that is released is repaid upon death, giving parents a boost to their income, without having to repay it while still alive. This allows parents to lend or gift a deposit to their offspring, with no financial implications until the end of their life. Ultimately, it will allow parents to know that they have helped their children and see that benefit, rather than it happening due to an inheritance after their death.

While the equity release market is highly regulated and is shaking off its negative image, there is one downside. If the parents who release equity choose not to make any repayments on the equity they have released, the debt will increase. This will only affect their dependants on the will, so this may make these schemes offputting. Despite this, we believe that this is a small price to pay against the potential capital gain of a first time buyer being able to purchase a property sooner, rather than waiting to inherit capital upon the death of their parents.

The problem

with the Bank of Mum and Dad

The BOMAD has undoubtedly helped thousands of first time buyers climb the first rung of the property ladder.

The BOMAD has undoubtedly helped thousands of first time buyers climb the first rung of the property ladder. A huge number of people will be receiving help from their loved ones and it will make a major difference in their lives.

Despite this, the main problem associated with the rapidly growing BOMAD is that it is a symptom of, rather than a solution to, the housing crisis affecting the UK. Although assistance from parents helps to ease the pressure on first time buyers, it does nothing to act as a permanent solution to the problem.

The main problem lies in the fact that many parents are simply unable to contribute to their child's first home. In 2016 it was calculated that a family with an average level of wealth in the UK would have to put up around 64% of their net wealth to help their child buy in London. Ultimately, many see the ability to use the BOMAD to buy a home as little more than a lottery.

Hard working aspiring buyers tend to be left behind purely because they come from a family that simply can't afford to offer the financial aid necessary. While families in London give or lend, on average, almost £30,000, this number is almost halved in Scotland, with buyers receiving £15,500 in financial aid from their families.

It seems to be an unfortunate fact then, that while the BOMAD will be a helpful force for many, it will leave plenty more people behind. Unless the housing crisis gets better, we are likely to see little change in the operation of the Bank of Mum and Dad.

CALL US ON 020 3761 6942
OR EMAIL INFO@IMCFS.CO.UK