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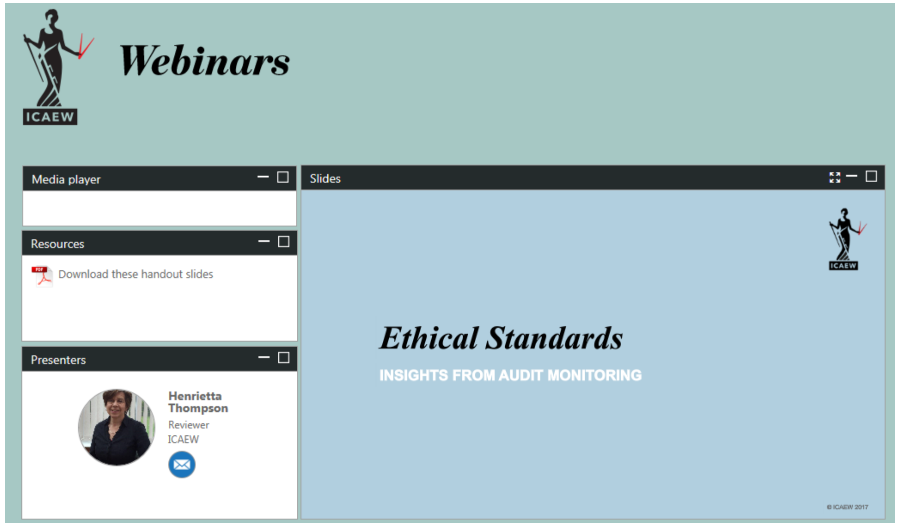

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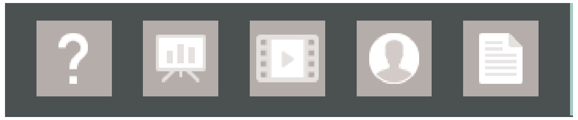

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Buy to Let is dead! Long live Buy to Let!

IN ASSOCIATION WITH KINNISON

FACILITATED BY JOHN GASKELL, HEAD OF PERSONAL FINANCIAL PLANNING, ICAEW

Property Investing Conference

02 December 2019

Are you a buy-to-let investor or are you thinking of retiring to the sun? Do you advise buy-to-let landlords or clients with overseas property? Get the latest insights on how to improve return on investment for you and your clients.

BOOK YOUR PLACE

Today's speaker

JATIN PATEL

FOUNDING PARTNER

KINNISON LIMITED

KINNISON
PROPERTY FINANCE EXPERTS

Buy to Let is Dead! Long live Buy to Let!

Jatin Patel

7 November 2019

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Agenda

1. Background
2. Regulatory changes in the Buy to Let Market
3. Buy to let lender landscape
4. Corporate landlords
5. ‘Alternative real estate assets’
6. Is Buy to Let Dead? Or Different?

KINNISON

Background – English Private Landlord Survey 2018 (published 2019)

- English Private Landlord Survey (EPLS) is a national survey (carried out in 2010 and 2018) of landlords and letting agents who own and/or manage privately rented properties in England.
- EPLS is an online survey of almost 8,000 landlords and agents
- Commissioned by the Ministry of Housing, Communities and Local Government

<u>Some of the findings from the EPLS</u>

Reasons for becoming a landlord:

- 46% prefer property to other investments
- 44% to contribute to their pension
- Only 4% to let property on a full time basis as a business

No. of Rental Properties	2018 %
1	45
2 to 4	38
5 or more	17

- Since 2010, the proportion of landlords:
  - with just one property has declined from 78% to 45%
  - with five or more properties increased from 5% to 17%

Background – English Private Landlord Survey 2018 (published 2019)

Landlords' Future Plans

- Landlords were asked what plans they had for their BTLs over the next 2 years:

	2010 %	2018 %
Keep the number of properties the same	84	73
Plans to increase the number of properties	12	11
Plans to decrease the number of properties	4	10

- The 10% of landlords planning to decrease the number of BTLs were asked to state their reason:

	2018 %
Legislative changes (e.g. to benefits, tax relief and stamp duty)	61
Personal reasons (e.g. approaching retirement age, other commitment etc.)	37

Regulatory changes in the Buy To Let (BTL) market

Prudential Regulatory Authority (PRA) introduced new stricter rules which took full effect in 2017

- New rules to ensure lenders are being prudent when assessing affordability and taking into consideration:
    - All costs (borne by landlord) associated with renting the property
    - Tax liability associated with the rental property
    - Potential risk of future interest rates rises
- Lenders applying the new rules to both refinances and new purchases
    - BTL lenders view the loss of interest deduction as an increasing cost for landlords
    - Affordability calculations for BTL are tightening
    - Consequently loan to values have dropped
- Introduction of a definition of a portfolio/professional landlord

Buy To Let affordability – purchase or re-mortgage (individual borrower)

	Basic rate tax payer (20%) Rental cover	Higher rate tax payer (40%/45%) Rental cover	Affordability stress test rate (less than 5 year fixed product)	Affordability stress test rate (5 year fixed product)
	125%	145%		
Max mortgage based on annual rent of £15,000	£218,182*	£188,087*	5.50%	
	£400,000*	£344,827*		3.0%**

* Subject to lender loan to value restrictions
** Actual pay rate

Certain lenders may allow income 'top slicing' to achieve higher loan to values

Buy To Let and 'Top-slicing'

- With the introduction of stricter affordability rules borrowers have had LTVs restricted where rental income has not be sufficient for the loan amount required
- Lender may be able to use the borrowers excess personal income to 'top-up' the rental shortfall
- Borrower will need to complete a detailed budget planner and clearly demonstrate the excess income
- Not all lenders will consider 'top-slicing'
- Not available to all types of landlords
- Lenders will restrict LTVs (irrespective of rental and personal income) typically to 75%

'Top slicing' is only available when borrowing in personal name

Regulatory changes in the Buy To Let (BTL) market – Professional Landlords

- According to the PRA professional landlords are defined as:
  - Borrowers with 4 or more distinct mortgaged buy to let properties (held in personal name or corporate)

- Lenders are required to carry out additional affordability checks on portfolio/professional landlords and take into consideration:
  - Property investment experience
  - Total amount of mortgage borrowing across all properties
  - Impact of new/additional lending on clients balance sheet
  - Income from both rental properties and other personal income

Regulatory changes in the Buy To Let (BTL) market – Professional Landlords

Lender requirements for Portfolio/Professional Landlords:

- Up to date detailed information on current BTL portfolio:
  - Type of property, number of bedrooms, full address (including post codes)
  - Rental income
  - Details of any outstanding mortgages eg lender, outstanding loan amounts, cost of debt, debt term
  - Current market value and purchase price of each property

- Business plan so that lenders can understand investment strategy, now and in the future. Should include:
  - What type of properties you buy and where
  - The type of debt used to acquire the properties eg interest only or capital repayment?
  - What is your exit strategy and timelines?
  - Do you have cash reserves to cover void periods?
  - How much do you spend on property maintenance and emergency repairs?
  - How much income do you receive on a monthly basis compared to your cost of finance?

Regulatory changes in the Buy To Let (BTL) market – Professional Landlords

How do lenders use this information?

- Evaluate your level of experience as a landlord and 'success'
- Analyse overall level and type of borrowing across the entire portfolio:
    - Highlight properties which have high LTV or negative equity
    - Assess whether you have too much debt
    - Assess whether you have the cashflow capacity to deal with interest rate rises and rental void periods
    - Evaluate the impact of additional loans on your overall debt position
- Understand your property business strategy and how you manage your portfolio
- Assess your expected future capital expenditure plans

How does this affect the lenders decision to lend?

- Coherent 'successful' investment strategy builds confidence in the credit case and underwriting process
- Lender may reduce (or refuse) the loan amount offered if they feel you are over-stretched

Buy to let lender landscape

- High street banks
- Building societies
- Regional building societies
- Specialist buy to let lenders (banks and non banks)
- Challenger banks
- 2nd Charge lenders (banks and non banks)
- Bridging specialists lenders
- Private banks (with or without AUM)
- Private funds

Buy to let lender landscape – public sourcing

- High street banks and building societies offer their products through direct access or market comparison websites

- Market comparison websites have limited information:
  - Loan to value (LTV)
  - Interest rates
  - Arrangement fees
  - Early repayment charges

- Such websites do not detail lender specific restrictions:
  - Type of tenant eg HMOs, air bnb, corporate let, single AST
  - Type of landlord eg professional or first time
  - Rent to buy
  - Type of property eg ex local authority, new build
  - Residency of landlord – UK/overseas
  - Structure of legal and beneficial owner of the property
  - Treatment of multiple properties

Buy to let lender landscape – sourcing

- Outside market comparison websites little transparency exists leading to increased reliance on brokers for:
  - Market knowledge and experience
  - Expertise to understand lender criteria, policies and procedures
  - Experience in dealing with credit officers/committees

- Most specialist, 2nd charge and bridging lenders do not appear on mainstream sourcing systems

- **Some specialist lenders, eg Bridging specialist lenders, Private banks or funds may restrict access to their product platform to specific trusted brokers**

- **Some lenders restrict the availability of certain BTL products to borrowers ONLY through brokers**

Mortgage finance implications – Corporate ownership

- Not all lenders are comfortable lending to corporate structures
- Greater appetite to lend to UK corporates rather than offshore
- Such mortgage lending can often have higher arrangement fees and interest rates
- Lenders are highly likely to request personal guarantees from shareholders/directors
- Some lenders may restrict loan to values (LTVs)
- Mortgage contract will be in the name of the corporate borrower
- Adverse credit history of shareholders could affect ability to raise finance
- Tax residency of underlying shareholders/ultimate beneficial owners is critical

Landlords – is incorporation the answer?

Implications for mortgage finance:

- Lenders may seek clarity on whether all related taxes (CGT and SDLT) have been paid
- If borrower is relying on tax reliefs lenders may request evidence of:
  - HMRC acceptance/clearance
  - Liquid funds to pay the taxes in the event of HMRC investigation
- You are likely to need consent from your existing lenders
- Lenders may charge a higher rate of interest and potentially higher arrangement fees
- Lenders are likely to request personal guarantees from all shareholders

Issues for landlords to consider:

- Potential lower LTV due to higher interest cost and banks' stress tests
- Whether potential higher arrangement fees and interest cost make financial sense
- An adverse credit report for any shareholder could prevent future finance/refinance applications
- Future impact on shareholders to personally raise finance
- Corporate Interest Restrictions rules

UK Corporate ownership – purchase or re-mortgage

	UK Corporate			UK Individual
	Rental cover	Affordability rate (less than 5 year fixed product)	Affordability stress test rate (5 year fixed product)	Higher rate tax payer (40%/45%) Rental cover
Capital raise/refinance	125%			145%
Max mortgage based on annual rent of £15,000	£218,182*	5.50%		£188,087*
	£400,000*		3.0%**	£344,827*

* Subject to lender loan to value restrictions

** Actual pay rate

UK Corporate ownership

2018 English Private Landlord Survey asked landlords how they own their properties:

How properties are owned	2010 %	2018 %
Individual	89	94
Corporate	5	4
'Other'	6	2

- 2018/19 tax return and payment deadline is 31 January 2020
- Full impact of interest deductability restrictions from April 2020

Implications for finance

- Landlords should review their existing finance arrangements to assess whether:
  - Finance costs can be reduced
  - Finance costs can be fixed to mitigate the risk of interest rate rises
- Application process for professional landlords will take longer given the amount of information required
- The approval/underwriting process may take longer as all the information needs to be evaluated
- Landlords need to find the right lender which fits their personal circumstances
- If landlords are considering changing ownership to corporate they need to review existing and future finance requirements
- Understanding the landlords' strategy becomes critical when evaluating the finance terms eg 2, 3 or 5 year fixed rates

Challenges faced by landlords

The economic returns for landlords have been under ‘attack’ from:

- Tax changes:
  - Interest deductability
  - SDLT
- Mortgage finance regulatory changes
- Costs associated with increasing legal obligations:
  - Registering with local council
  - Tenant Fees Act
- Increased competition from:
  - Developers retaining inventory for rental
  - Build to Rent / Private Rented Sector
- Stagnant/falling rent

To mitigate these head winds some landlords have started looking at ‘alternative’ real estate assets

‘Alternative’ real estate assets

- Changing geographical location:
  - Lower initial capital expenditure – impacts SDLT/deposit
  - Potential for higher annual rental increases
  - Rental void periods maybe longer
- Acquiring assets (at ‘undervalue’) which are dilapidated and require expenditure prior to rental
- Developing existing assets to increase rental income:
  - Loft conversions
  - Property extensions
- Changing tenant type (and consequently rental income)
  - Air bnb/student accommodation/HMOs
- Changing asset type:
  - Mixed use – eg ground floor commercial and residential above
  - Pure commercial

'Alternative' real estate assets – finance implications

- Where landlords are considering 'changing their tenant type' they need to review existing debt contracts to ensure they are not in breach of the mortgage agreements

- If landlords are thinking of acquiring 'alternative' real estate assets then they need to properly research their finance option:
    - Conventional mortgages may not be appropriate for such assets
    - Not all main stream lenders will lend against such assets
    - Finance costs and arrangement fees tend to be higher than for conventional mortgages

- How will extensive refurbishment/development costs affect the value of the property and implications for refinance?

- If property is in severe disrepair it may not be suitable for a mortgage

- For pure commercial assets valuation is critical and can be affected by
    - Type and quality of tenant
    - Strength of covenants in tenancy agreements etc

‘Alternative’ real estate assets – finance implications

How have lenders reacted to the challenges landlords face?

- Significant increase in the number of BLT products
- More lenders entering the 5 year fixed market
- Increase in competition has lead to cost of finance falling
- Lenders have been more innovative in their product offering:
    - Refurbishment BTL product
    - ‘Top slicing’
    - Extending their current offering to cover HMOs and student accommodation
    - Fixed arrangement fees
    - 2nd charge lending to facilitate development work

Is Buy to Let Dead? Or Different?

- Since the last Private Landlords Survey (PLS) was undertaken in 2010, the private rented sector has undergone substantial growth and change.

	2010-2011 Millions	2017-2018 Millions	% Increase
No of households renting	3.6	4.5	25
No of families renting	1.1	1.6	45

Source:English Housing Survey Headline Report 2017-18
Household: One person or a group of people (not necessarily related) who have the accommodation as their only or main residence eg couple with or without children, lone parent with children

Demand for rental properties continues to be strong however landlords need to be innovative and flexible in their approach and need to consider:

- Ownership structure
- Type of properties and tenants
- Sources of finance
- Location of properties

How Kinnison can support you

- Research the **whole of market** and discuss with you the potential financing options for your property transactions

- Help you prepare to apply for a mortgage:
  - Guidance on checking your credit score
  - Collate relevant 'know your client' documentation
  - Collate supporting documentation

- Assist professional landlords to understand and collate the detailed information required for their mortgage application

- Reviewing your business plan and support you in preparing a coherent credit case

With our banking experience we are uniquely placed to understand the lenders credit approval process and assist landlords through the process

How Kinnison can support you

After the application has been submitted:

- Answer any questions that the lender/underwriter may have

- Understand your mortgage offer/conditions:
  - Interest rate, mortgage term, monthly repayment terms and amounts
  - Conditions for overpayment, fees, early repayment charges
  - Payment holidays
  - Total cost of borrowing

- Assist you through the completion of your mortgage/purchase/refinance
  - Liase with lender
  - Interact with valuers/solicitors

How Kinnison can support you

Through our partnership with the ICAEW we have a dedicated mortgage advisory service for ICAEW members through Kinnison Mortgage Services ("KMS") offering at a significantly discounted fee structure:

Fee structure	Service
Retail banks and building societies (mortgages <£750k) ➢ Fee of £199 on application and £299 on completion ➢ No further fee payable ➢ Kinnison will receive a fee from the lender	➢ Whole of market access ➢ Real time access to products and rates ➢ Deep understanding of lenders affordability and repayment criteria ➢ Time efficient

Fee structure	Service
Private banks and specialist lenders (mortgages > £750k) ➢ Kinnison standard fee of 1.1% reduced to 0.6% of the finance arranged ➢ Kinnison may receive a fee from the lender, which, if received will be rebated against the 0.6% client fee	➢ Access to an opaque mortgage market ➢ Bespoke and negotiated terms, conditions and pricing ➢ Preparation of full credit paper ➢ Understanding of the credit officer approach

- Is it possible to make money from property?

- Case Study driven workshops delving deeper into the issues faced by landlords whilst raising finance, in particular looking at:

  - Single or multiple residential buy to lets

  - 'Alternative real estate' assets

QUESTIONS?

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Join the ICAEW Personal Financial Planning (PFP) Community: www.icaew.com/pfp

Other ICAEW events:

- ***ICAEW Property Investing Conference 2019***

  Full day conference: 2 December 2019, 09:00-18:00
- ***Wills & Inheritance Tax Planning***

  Workshop: 19 November 2019, 09:00-15:30

  Venue: Ironmongers Hall, London EC2Y 8AA
- ***Webinar: 'Buying a property overseas'***

  19 November 2019, 09:00-18:00

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