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Mortgage affordability assessment

Are you financially prepared to apply for a mortgage?

Are you financially prepared to apply for a mortgage? This is a question that countless prospective homeowners grapple with each year. Succeeding in this process brings you significantly closer to your dream of homeownership, whereas falling short may require reassessing your plans.

This affordability assessment evaluation is structured to ensure you can consistently meet your monthly mortgage payments. Consider it a meticulous examination of your finances, scrutinising your ability to afford the desired home loan.

Lender's decision-making process

Embarking on a mortgage application involves more than just evaluating whether you can manage the monthly repayments. Mortgage providers scrutinise your income and expenditure to determine if you can keep up with repayments if interest rates escalate or circumstances shift.

The loan-to-income ratio is a key element in a mortgage lender's decision-making process. This figure is derived by dividing the amount you intend to borrow by your annual earnings. Typically, the maximum amount you can borrow is capped at four-and-a-half times your yearly income.

Anticipating life changes

Lenders are also responsible for evaluating the monthly payment you can feasibly afford. This assessment, known as the 'affordability assessment', considers both your income and outgoings. Lenders must make future projections and conduct a 'stress test' on your ability to repay the mortgage.

This practice helps ensure you can still afford payments if the interest rate increases or your lifestyle significantly changes. Such changes could include redundancy, having a baby or deciding on a career break. If a lender believes these circumstances could jeopardise your ability to meet mortgage payments, they may limit the amount you can borrow.

Assessing your earnings

Your income is a key factor in determining your borrowing capacity for a mortgage. This includes not just your basic earnings but also income from pensions or investments, child maintenance and financial support from ex-spouses, and any additional earnings you may have. Such extra earnings could come from overtime, commission, bonus payments, or income from a second job or freelance work.

Proving your income

You must provide documents like pay slips and bank statements to validate your income. However, if you're self-employed, the process becomes more thorough. You'll need to provide documents such as your bank statements, business accounts and details of the Income Tax you've paid. Lenders typically require two to three years' worth of tax returns and business accounts.

Evaluating your outgoings

Your outgoings will significantly affect your ability to borrow. These include credit card repayments, maintenance payments, various types of insurance (building, contents, travel, pet, life, etc.), any other loans or credit agreements you might have, and bills such as water, gas, electricity, phone and broadband.

Estimating your living expenses

In addition to your fixed outgoings, lenders might ask for estimates of your living costs. This could include spending on clothing, basic recreation and childcare. They might request to see some recent bank statements to verify the figures you provide.

Preparing for future uncertainties

It is crucial to consider future changes affecting your ability to repay your mortgage. Lenders will assess whether you'd be able to meet your mortgage payments if situations such as an increase in interest rates, job loss, illness, or significant life changes like having a baby or taking a career break were to happen.

Planning for the unexpected

Planning is also crucial to preparing for a mortgage. This includes considering how you'd meet your payments in case of unexpected financial changes. One way to protect yourself against unexpected drops in income is by building up savings when possible. Aim to save at least enough to cover three to six months outgoings, including your mortgage payments. ■

Do you want to discuss your options with a professional mortgage expert?

If you require further information or have any questions about the mortgage application process, please get in touch with us. Our team is here to provide the necessary support and advice to help you navigate this important financial decision. To discuss your mortgage options or for more information, please contact us.