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Financing Your Property Business - A Landlord's Perspective By Richard Blanco

Please note: this is a landlord/developer's perspective, you should always seek professional advice on financial matters. Details correct in August 2012.

Are you clear about your business model? There are a number of key concepts that are at play here. For each property purchase, you need to consider cashflow versus capital growth. Ideally all of your properties will give you both, but sometimes it's worth buying a property that will boost one or the other. Enough cashflow properties will enable you to live off your property business and enough capital growth will give you long term financial security. You also need to be clear about your target market - that is type of tenants, the types of properties you want to purchase and the geographic areas you want to focus on. These three concepts are interdependent. So if you want to focus on high end corporate lets for example, they will probably need to be in a central location close to transport and probably contemporary new builds or very smart conversions.

When considering funding, I think it's really important to devise a strategy and write it down. I recommend creating a five year business plan, set goals in terms of your portfolio size and rental profits. This will help you make decisions and present your case to lenders.

The first port of call for landlords is mainstream buy to let lending, of which there are many advantages. Quite a lot of lenders have returned to the market and these products are great for properties that are let or ready to let. Loan to value (LTV) is improving, with 75% routinely available now and some 80% and 85% LTV products. Rates improved considerably in 2011 and in 2012 there are many products in the 3.5% to 4.5% range. You don't have to go to brokers, many products are available direct from banks and building societies.

On the flip side, many products with low headline rates charge high arrangement fees - tantamount to confusion marketing, so you will need to compare two year products by working out the total cost over two years. Some mainstream lenders are slow, two of my recent remortgages took 3-4 months to complete. Pre 2008, good rates were routinely available at 85% LTV, now rates on these types of products are uncompetitive. Valuations can be the biggest challenge with mainstream lenders, particularly if your buying a property that needs refurbishment. A lack of kitchen and bathroom will deem the property as uninhabitable and outside of criteria and if the property is in poor condition the rental valuation will be downgraded and it will no longer fit criteria. You are also subject to the whims of the valuer that is allocated to you especially as some have a better knowledge of rental valuations than others. In some parts of the UK and depending on the economic cycle, valuers may err on the side of caution and this can scupper your mortgage application, having already wasted a footprint on your credit file. So only go for mainstream funding if you are sure you will get through all the hoops.

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Of course, brokers can be very helpful in guiding you through this process and maximising the possibility of success.

With mainstream lenders, there are an increasing number of "trip you up criteria." The six month rule means that you cannot remortgage a property until you've owned it for six months and indeed the vendor must have owned the property you're purchasing for six months for you to get a mortgage. Lenders got burned pre credit crunch and this is their sledge hammer approach to preventing same day remortgages and dodgy flipping. Most of us didn't get involved in that kind of stuff but I'm afraid the lenders have tarred us all with the same brush. This rule primarily affects landlord developers who buy wrecks, refurbish them and then want to refinance their cash out of the deal.

Another spin off from the six month rule is that an increasing number of lenders apply capital raising restrictions. So for example you may not be able to capital raise until you've had the mortgage for 12 months. Some lenders restrict he maximum loan to the valuation of the property at purchase plus the cost of any works. There may be a lower LTV restriction on further advances or the purpose of capital raising might be restricted to home improvements.

Other frustrating criteria includes a cap on the number of properties you can have mortgaged with one lender, restrictions on the total number of properties you have regardless of lender, restrictions on housing sharers or students, HMOs and multiple units like two flats in one house. Most lenders have a minimum income requirement between £20,000 and £50,000 per annum - typically £25,000 and there may be restrictions on how much of this can be salary, dividends, bonuses, earnings from property etc. Where there is no minimum income requirement, lenders will very likely use credit scoring, so it's worth considering some of the factors that will affect your credit score.

Once upon a time, paying all your bills on time and not applying for too much credit meant you had a great credit score. This is no longer true. You need to manage your credit score and you can do this using one of the services like www.creditexpert.co.uk. Some examples of factors that will enhance your score are: obviously not having any missed payments and being on the electoral register, but also having a recent mortgage for more than 12 months, no recent searches on your file, having a high credit card limit on one of your cards, having accounts for a long time and successfully settled accounts. Negative factors might be the balance of your unsecured lending - usually credit cards and the usage of your available credit. Also a history of mail order accounts or payday loans has a negative effect.

Where mainstream banks and building societies require a minimum income they will often do a credit search that just looks for adverse credit - that is missed payments. Others, especially high volume buy to let lenders that do not require a minimum income will use complex credit scoring schemes. You will often need a higher score for higher

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LTV products. Note the difference between quotation and application searches on your credit file. An application search will be made when you make your application. You need to have a s few of these as possible in any six month period. This is because application searches are shown to other lenders who will assume you are making lots of applications for credit and therefore are a higher risk. Quotation searches, sometimes called soft footprints, are not seen by other lenders. I recommended having a discussion with your lender about the type of search they will make and managing this carefully. I recently asked a lender not to carry out a credit search until the valuation had been carried out. Sure enough the valuer gave too low a figure for me to want to proceed so I withdrew my application without having suffered an application search on my credit file.

Other factors that will affect your score: common ones are a discrepancy with your electoral role information or your financial connections with other people. Note that having 0% balance transfers on credit cards can lower your credit sore. Imagine the credit limits on all of your credit cards total £20,000 and you have a £10,000 0% balance on one credit card. The lender will assume that because you are using 50% of your available unsecured credit, you are credit hungry and therefore a higher risk. The fact that you may be wisely parking a small amount of debt at 0% does not compute I'm afraid! It's a very flawed system because lenders encourage us to use debt and then when we do so we are automatically seen as a higher risk. The moral of this tale is that it is always best to hold debt as secured borrowing - i.e. in mortgages.

Getting funding for development, including refurbishment is still a challenge. There were many light refurbishment products pre-2008 but now the only one available is through The Mortgageworks. An alternative is commercial lending through a high street bank, where you meet a commercial or sometimes property specialist and discuss your plans. LTVS are rarely higher than 65% and there will be few, if any, interest only options. But where buy to let lenders can be a bit rigid, commercial lending may be much more flexible and tailored to your business needs. Many developers who need cash to move their business forward are using bridging finance, which has become increasing competitive. Although arrangement and exit fees were common, you can now get products that charge 1% per month with no fees. Because of the six month rule, you should usually plan to be in the loan for up to 8 months, allowing two months to process the buy to let mortgage afterwards. Never take out bridging finance without having an exit strategy.

Again portfolio lending was common pre-2008, but many high street banks now have "no appetite" for this type of lending or will set high minimum loan thresholds of around £1.5m. Again LTVs are much lower than they were historically, though this is often relationship dependent. Some private banks for example will be happy to lend to loyal customers with far fewer restrictions.

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The final issue to consider is your home loan and your earnings. Residential mortgages - on the place where you live - are usually restricted to around 4.5 times gross income. Many property professionals will have a mixture of income sources including income from property, a salary, bonuses, plus dividends and company profits if they have a limited company. Lenders differ as to what they will and won't allow as income for mortgage purposes. An increasing number of borrowers are 'mortgage prisoners' with their home loan because they can no longer raise the same level of residential borrowing on their current income. This can be doubly frustrating as it restricts your ability to make full use of the equity in your home.

A good rule of thumb is that you need to ensure £25,000 of income from sources other than property to fulfil buy to let lender's criteria. Another point to note is that there has been an erosion of interest only products with a number of lenders restricting interest only loans to 50% LTV.

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