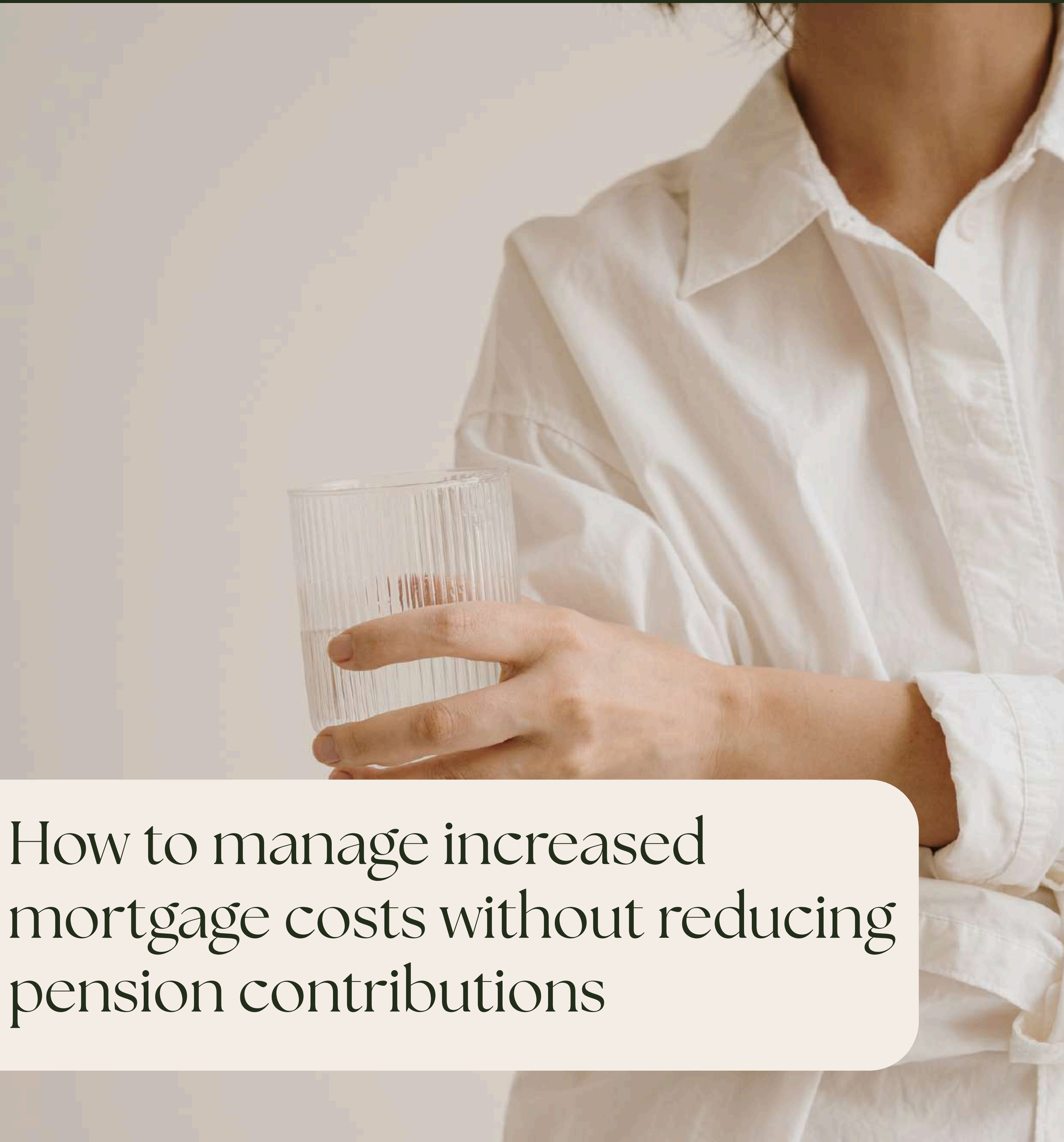
EVA WEALTH

Smart Money, Strong Women

Chartered Financial Planner



How to manage increased mortgage costs without reducing pension contributions

01935 315611

hello@evawealth.co.uk

How to manage increased mortgage costs without reducing pension contributions

23% of people said they would reduce pension contributions to cover increased mortgage costs. Read about why this may not be a sensible choice.

In April 2021, the average price of a pint of milk was 42p, according to the Office for National Statistics (ONS) [1]. By April 2023, it had risen to 68p.
You've likely seen headlines about high inflation and the rising cost of essentials like food and fuel—and may have felt the impact on your own monthly expenses.
However, the rising cost of groceries and fuel might not be your biggest concern. High inflation is also driving up interest rates, which could lead to increased mortgage repayments—if they haven't gone up already.

Over 1 million households could pay an extra £500 a month by 2026

Inflation has remained above the Bank of England's (BoE) 2% annual target for over two years. According to the ONS [2], it stood at 7.9% in the 12 months to June 2023.

In response, the BoE has implemented measures to bring inflation back down to target. One of the main tools it uses is increasing interest rates. When this happens, banks, building societies, and other financial institutions typically raise their own rates, making borrowing more expensive. At the same time, savings account rates improve, encouraging consumers to save rather than spend.
This reduction in spending can decrease demand for goods and services, which helps slow down price rises and, ultimately, reduce inflation.

To combat persistently high inflation, the BoE [3] has raised its base rate 14 consecutive times since 2021, reaching 5.25% on 3 August 2023. Mortgage rates have been climbing in tandem.
According to Rightmove [4], the average interest rate on a two-year fixed mortgage with a 95% loan-to-value (LTV) ratio was 6.94% as of 31 July 2023—a sharp rise from the 1.99% average reported by Moneyfacts [5] in July 2020.

As fixed-rate mortgage deals come to an end, many households may face a substantial jump in monthly repayments. In fact, The Guardian [6] reports that more than 1 million households could end up paying an extra £500 a month by 2026.
As a result, you may need to reassess your budget to accommodate these increased mortgage costs.

23% of people said they would reduce pension contributions to pay increased mortgage costs

A survey reported by Mortgage Solutions [7] found that 23% of individuals with assets of £250,000 or more said they would reduce their pension contributions to cope with higher mortgage costs. While this might help manage a larger monthly mortgage payment, it could mean missing out on valuable compound returns on your pension savings.

More importantly, you may not be able to compensate for those missed contributions later in life, potentially resulting in a smaller retirement fund. In fact, stopping pension contributions for just one year could mean up to £13,000 less in retirement savings.

You might think that pausing or reducing contributions for a short period won't make a big difference in the long run. However, a study from Standard Life [8] suggests otherwise. Their figures indicate that halting contributions for one year at age 35—assuming you began saving at 22—could leave you with almost £13,000 less in your pension pot by age 68.

And since no one can predict how long interest rates will remain high, adopting this strategy could mean stopping contributions for even longer than planned.

The table below illustrates the potential impact on your pension if you began contributing at age 22 with a salary of £25,000, based on minimum auto-enrolment contributions (3% employee and 5% employer):

How pausing pension contributions could affect your total retirement savings				
Length of time that pension contributions are stopped for	No breaks or reductions in contributions	Stopping contributions for one year at the age of 35	Stopping contributions for two years at the age of 35	Stopping contributions for three years at the age of 35
Total retirement fund at age 68	£456,893	£444,129	£431,558	£419,180
Potential loss in savings	£0	-£12,764	-£25,335	-£37,713

Source: Standard Life [9]

So, as you can see, stopping or reducing pension contributions could harm your financial plan in the long term.

Fortunately, there are alternative ways to manage those additional costs without disrupting your retirement plan.

5 ways to deal with increased mortgage costs without reducing your pension contributions

If you are concerned about rising mortgage costs, you may want to speak to your lender as soon as possible

2. Speak to your Lender

If you're concerned about rising mortgage costs, it's a good idea to speak to your lender as soon as possible. In many cases, they'll work with you to help make your payments more manageable.

For instance, they might offer a payment holiday or a temporary reduction, allowing you to continue meeting your monthly obligations.

It's important to have this conversation early, so you can agree on a solution before missing any payments. Failing to pay in full—without an arrangement in place—could negatively impact your credit score.

2. Switch to a better deal

Many people see their monthly payments rise when their fixed-rate mortgage ends, as lenders typically move them onto a standard variable rate (SVR), which is usually higher.
In fact, the average SVR is currently 8.49%, according to Uswitch [10]—significantly above the average fixed-rate mortgage interest rate.
If you're no longer on a fixed-rate deal, or yours is ending soon, it may be worth exploring your options to secure a lower interest rate. Even though rates remain relatively high, you might still find a more affordable alternative—especially if you're currently paying the SVR.

3. Consider switching to interest-only

If moving to a better deal isn't an option, you might consider speaking to your lender about switching to an interest-only mortgage. This can reduce your monthly payments, as you're only paying the interest—not the loan amount itself.
For example, on a property worth £286,000—the average UK house price in July 2023, according to the ONS [11]—with a 90% loan-to-value (LTV) ratio and a 6% interest rate, your monthly payment would be £1,824.47 (based on MoneyHelper's [12] mortgage calculator). Switching to an interest-only mortgage would lower that to £1,415.70.
However, keep in mind that this option doesn't reduce your debt. You'll still need to repay the full loan in the future, either through ongoing payments or when you sell the property.

4. Extend the term of your mortgage

Extending the term of your mortgage can lower your monthly payments, as the loan is spread over a longer period.
Using the same example as before, a mortgage with a 25-year term would have monthly payments of £1,824.47. If you extend the term to 40 years, the payment drops to £1,557.87.
However, this option may not be available if you're on a fixed-rate mortgage. It's also important to consider the long-term impact: while the interest rate stays the same, paying it over a longer period means the total interest paid will be significantly higher.

5. Speak to a mortgage broker

Choosing the best course of action can be challenging, as each option has its pros and cons. Before making any changes, it's important to consider not just how it affects your monthly mortgage payments, but also the impact on your long-term financial goals.
With that in mind, speaking to a mortgage broker could be a wise step. They can help you navigate rising mortgage costs and may have access to deals that aren't widely available to the public. Let us know if we can help you with this.

Important Note

A pension is a long-term investment and is not usually accessible until age 55 (rising to 57 from April 2028). The value of your pension can go down as well as up, which may affect the benefits you receive.

Past performance is not a reliable guide to future results.
Tax treatment of pension withdrawals depends on your individual circumstances and may change in the future, as thresholds, rates, and legislation are subject to revision.

Your home may be repossessed if you do not keep up repayments on your mortgage or any other loans secured against it.

SOURCES

Buy-to-let (pure) and commercial mortgages are not regulated by the FCA.

Think carefully before securing other debts against your home.

[1]03.08.2023 Ave. price – milk: pasteurised, per pint Office for National Statistics

[2]03.08.2023 Consumer price inflation, June 2023 Office for National Statistics

[3]03.08.2023 Official Bank Rate history Bank of England

[4]03.08.2023 What are the current UK mortgage rates? Rightmove

[5]03.08.2023 2020 mortgage interest rates review Moneyfacts

[6]03.08.2023 Mortgages to cost 1m borrowers extra £500 a month by 2026, Bank warns the Guardian

[7]03.08.2023 Homeowners cut pension contributions to pay rising mortgage bills Mortgage Solutions

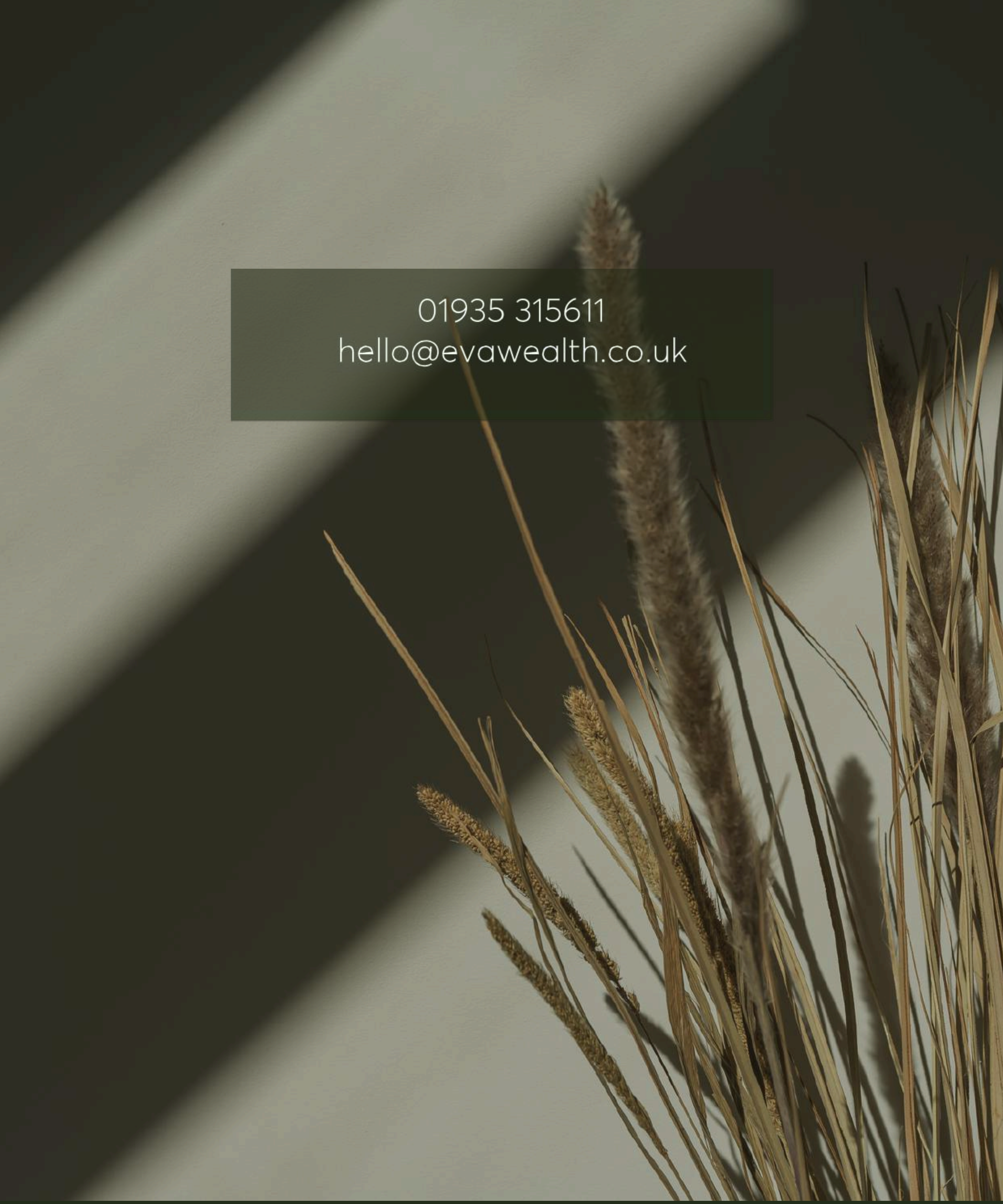
[8]03.08.2023 Standard Life highlights the long-term implications of pausing pension contributions during the cost of living crisis Standard Life

[9]03.08.2023 Standard Life highlights the long-term implications of pausing pension contributions during the cost of living crisis Standard Life

[10] 03.08.2023 Compare mortgages Uswitch

[11]03.08.2023 UK house price index May 2023 Office for National Statistics

[12]03.08.2023 Mortgage calculator MoneyHelper



01935 315611
hello@evawealth.co.uk