



CENTRE FOR THE STUDY OF FINANCIAL INNOVATION

5 DERBY STREET
LONDON W1J 7AB

TEL: 020 7493 0173
FAX: 020 7493 0190

The future of the UK mortgage market: The Mortgage Market Review, the FSA's proposals on responsible lending, and the future of the housing finance industry. A round-table discussion with Michael Coogan (Council of Mortgage Lenders), Sheila Nicoll (FSA), Stephen Blackman (RBS) and Iain Laing (Santander).

**To be held on Wednesday, October 13, 2010, from 12:30-2:15pm.
At Innholder's Hall, 30 College St, London, EC4R 2RH.**

The round-table on the future of the UK mortgage market attracted a large audience, an indication of the extent to which a significant portion of the UK has an interest in what happens in the housing market. The discussion centred on the direction of the FSA's Mortgage Market Review (MMR) and its potential impact on current and future mortgage holders.

One speaker noted that both the FSA and the industry shared an interest in ensuring a sustainable and flexible market for mortgage finance. He felt, however, that the MMR – in its current form – would not achieve that and that the section on responsible lending, in particular, should be withdrawn as the potential knock-on effects for current and future borrowers far outweighed any presumed benefits.

He stated that the market had actually 'self corrected' since the Review began and that excess capital had not and would not return to the market. He went on to say that even the FSA agreed that the mortgage market had worked well for the majority of borrowers and what was being proposed was a major intervention into a market that had (largely) worked well. Another member of the panel disagreed and felt that the market had not been working well and that banks had benefited from a large injection of public funds.

One member of the panel felt that the current level of arrears, for example, was not a result of irresponsible lending but evidence of the impact of the recession and the consequent change in borrowers' circumstances. Arrears were, as highlighted by another panellist, lower than they had been in the 1990s (and past their peak) despite a sharp fall in house prices. Approximately 2% of borrowers were currently in arrears. The figure for first time buyers (from 2005-2009) was slightly higher at 5% but for both groups the vast majority of borrowers were servicing their debt even in a difficult economic environment.

One participant noted that the potential impact of a rise in interest rates on arrears had to be considered. However, another said there were many consumers on fixed-rate mortgages who had not benefited from interest rate declines and had continued servicing their loans. **Another attendee? Another panellist, or an attendee?** suggested that the potential loss of one million lost jobs would put upward pressure on arrears and one of the panellists pointed out that there was a lot of forbearance in the

market at the moment. Another speaker said that had already been accounted for in the arrears statistics. Unemployment, interest rates and government support were being analysed for their potential impact on arrears but it was a public policy question as to what was the appropriate response.

If, for example, the proposed FSA rules had been in place, significant numbers of existing customers (the majority of whom were currently servicing their loans) would not have been given mortgages. Was a risk-averse mortgage market desirable; protecting the minority but having a negative impact on the majority? For current borrowers, the speaker felt that the proposed rules risked 'trapping' them in their present mortgages given the likely decline in choice and eligibility for new loans. This was on top of the potential costs to lenders of implementing new prudential rules and regulatory changes.

The speaker felt that the impact on future lending had not been adequately analysed by the FSA and that the responsible lending proposals were fundamentally flawed. The few rules that may have added value had been lost in the rules over affordability and did not represent the type of proportional intervention that the speaker felt was needed. Another speaker felt that aspects of the MMR went beyond current best practice on, for example, income verification and said practices such as credit scoring worked well.

Two of the panellists felt that crude rules would force lenders to decline applications that would probably perform well and did not account for the ways in which borrowers adjusted and 'squeezed' their expenses (particularly in the early years of their loans) in order to afford to buy a home. Nor was there any credit for the rational decisions that borrowers took when deciding, for example, that the benefits of an interest-only mortgage outweighed what they would pay out in rent. In addition, the FSA approach would make it very difficult for those with variable incomes to secure mortgages. Looking at the shift in employment patterns, the number of people who were self employed was increasing. As a result there would be a rise in the proportion of people who would find themselves ineligible for mortgages.

This tightening of credit criteria, in the context of a decline in the overall availability of credit, could have a big impact and public debate was needed. The paradox was that it could turn out to be quite good for the big lenders. The broker market would be undermined as it would be more difficult to move mortgages and the mortgage market would be less competitive. From a broader perspective, one had also to consider the material impact on house prices and the economy.

One of the speakers felt that the FSA was taking a common sense approach and that some of what it was proposing had been misunderstood. It was not looking to ban particular types of mortgage (such as interest-only) but was keen to maintain an evidence-based approach that dissuaded borrowers from over-stretching. The FSA was conscious of market conditions and pressures, and implementation would take those into account.

One of the attendees noted that perhaps not all lenders had been as responsible as some of the speakers were describing. A member of the panel felt that, yes, there had been outliers but that they illustrated the failure of supervision and not a lack of

adequate rules. Another speaker said that while there had been risky lenders, most had gone out of business by now. And, in fact, 90% of all lending was done by just six banks,

Another speaker felt there was wide support for a 'boring' housing market with stable prices. She said a lot of the lending over the past few years had been for buy to let and re-mortgaging rather than home ownership. One of the other panellists, looking at the long-term, felt there was a larger question that needed to be addressed. Namely, if people did not become homeowners, where would they live? This was a housing policy issue that needed to be addressed by government. Another speaker agreed that there was a broader debate to be had on housing but felt that it was less of an issue of where people lived, rather that they perhaps might live in smaller houses.