Mortgages

Product Sales Data (PSD)

Trend Report | 2005-2012

August 2012

Mortgages Product Sales Data (PSD)

Trend Report 2005-2012

August 2012

Contents

1. Highlights 2011-2012 2

2. Introduction 2

3. What is product sales data (PSD)? 2

4. Interpreting the data 3

5. What information is available from mortgage PSD? 3

6. How does mortgage PSD compare to other published data? 3

7. The overall trend in mortgage sales 3

8. The characteristics of new mortgage sales 6

   8.1 Borrower type – number of sales 6

   8.2 Remortgage purpose 7

   8.3 Lending spreads 8

   8.4 Types of interest rate 8

   8.5 Repayment method 9

   8.6 Loan to value (LTV) ratios 10

   8.7 Income verification and risk-based lending 11

   8.8 Mortgages to borrowers with impaired credit history 12

   8.9 Income multiples 12

   8.10 Lifetime mortgages 12

   8.11 Sales channels 13

   8.12 Advised sales 13

9. A closer look at first-time buyers 14

10. Regional analysis 16

11. Appendix 17

1. Highlights 2011-2012

Overview of the mortgage market

- Economic and financial conditions during the period under study were unsupportive of the mortgage market; real disposable income declined, unemployment rose, and the UK economy re-entered recession. The intensification of the euro area sovereign crisis raised funding costs for mortgage lenders, some of which has been passed on to consumers. This, together with the still uncertain economic outlook and limited availability of wholesale funding, has caused banks to tighten lending criteria.
- Mortgage sales between 1 April 2011 and 31 March 2012 recorded a modest increase of 3.7% versus 2010/11. This is in line with the rise in both the number of selling firms and provider firms during the same period.
- Most mortgages were provided by banks (69%), followed by building societies (18%). Building societies have gained market share in 2011/12 while those of banks and their subsidiaries have declined. The mortgage market remains concentrated: in 2011/12, the top five providers accounted for about 64% of all sales by volume, the top ten for 86%, and the top twenty for 94%.
- Intermediaries have maintained their market share during 2011/12, while firms selling directly to customers have lost market share. Mortgage sales for intermediaries expanded by 8% versus the last fiscal year, while direct sales remained broadly unchanged.
- The proportion of advised sales continued to increase in 2011/12. As intermediaries tend to sell with advice (98% of sales in Q1 2012 versus 48% for firms selling directly to customers), this is consistent with their solid performance. The increase in the number of products may also have benefitted intermediaries more than providers selling directly to borrowers since it widened the range of options available to them.
- Mortgage spreads (calculated as the difference between mortgage rates and the Bank of England base rate) declined in 2011/12 to 3.09% from 3.26% in 2010/11.

Trends within the mortgage market

- Across borrower types, mortgage sales to first-time buyers and remortgagers expanded significantly in the period under study, by 6.7% and 9.8% respectively, while sales to home-movers fell by 1.9%. The expansion for first-time buyers was assisted by the stamp duty exemption for houses costing up to £250,000.
- The rise in mortgage sales has been concentrated in the higher LTV (loan-to-value) bands, such as those above 75%. This is due to the role played by first-time buyers, who traditionally need higher LTV ratios and income multiples to step onto the property ladder.
- The proportion of income-verified mortgages has continued to grow in recent quarters and, at 74%, is now at its highest since data collection begun in Q2 2005. This is higher for first-time buyers and elevated LTV ratios.
- Fixed-rate mortgages expanded again in 2011/12 by 24.2%, while sales of mortgage products linked to variable rates declined. This increase in fixed-rates mortgages may have been aided by a fall in initial fixed rates during 2011/12.
- The move away from interest only products and into capital and interest repayment methods continues – especially for first-time and right-to-buy buyers.
- A north-south divide is also apparent in the number of new mortgages sold normalised by regional population. In Northern Ireland, only 9.8 mortgages per 1000 inhabitants were sold during 2011/12, while in the South West the ratio reached 21.9.

2. Introduction

In December 2005, we made a commitment to the industry to publish aggregate product sales data (PSD). We first published data in June 2007 covering the period April 2005 to March 2007. The last annual trends report was published in August 2011. We are also publishing PSD trends reports covering retail investments and pure protection insurance contracts.

In line with our commitment to greater transparency, we continue publishing the underlying data in accompanying tables on our website. These tables cover the seven-year history of the dataset (from Q2 2005 until Q1 2012). Our analysis focuses on those developments we deem most insightful when interpreting the main trends in the mortgage market.

If you have any comments on the content of this report, or suggestions on how we might improve future issues of the PSD reports, please contact us at: **product.sales@fsa.gov.uk**. We welcome your feedback.

3. What is Product Sales Data (PSD)?

Since 1 April 2005, product providers have been required to provide us with transaction-level data on all sales of regulated mortgage contracts, retail investment products and certain pure protection products to retail and private customers. This covers direct sales by firms' own sales forces and sales made by intermediaries. Between April 2011 and March 2012, some 720 unique firms provided PSD reports, with 259 reporting mortgages, 476 reporting retail investment products and 91 reporting pure protection products. Some firms report on more than one product area and a number of firms provide nil returns.

Reporting firms are required to submit quarterly PSD reports. By 31 March 2012 we had received PSD for 28 calendar quarters, accounting for over 35m transactions, including 19.8m retail investment products, 5.4m pure protection products and 10.5m mortgages.

PSD provides an important source of information that helps our risk-based supervision strategy. The nature of the data means we can use it at the detailed level to identify individual sales by firms and at the aggregate level to monitor product and market sales patterns.

4. Interpreting the data

Please note the following points.

1. This report focuses largely on the volume of transactions, not the value.
2. Some totals may show slight discrepancies due to rounding of figures.
3. Since 1 April 2006, all PSD reporting firms have been required to state whether customers received advice at the point of sale, therefore all analysis involving advised sales will be from this date onwards. For more information on what constitutes an advised sale, please refer to the appendix.
4. PSD only captures new sales (including remortgages); transfers, top-ups, alterations, increments and renewals are generally not included.
5. Some of the figures may be seasonally adjusted by applying the x12 filter.[1] Seasonally adjusted figures are followed by an '(s.a.)'.

5. What information is available from mortgage PSD?

Details of loans for house purchases and remortgages are captured by mortgage PSD, but data relating to further advances are not. Additionally, mortgage PSD only covers regulated mortgage contracts and therefore excludes products such as second-charge lending, commercial, and buy-to-let mortgages.

Only completed transactions (where the funds have been transferred from lender to borrower) are reported in mortgage PSD.

Definitions of terms relating to mortgage PSD are included in the appendix.

6. How does mortgage PSD compare to other published data?

The data submitted by each lender for mortgage PSD is the same as the data submitted to the Council of Mortgage Lenders (CML) for their Regulated Mortgage Survey. However, the figures published from the Regulated Mortgage Survey will differ from mortgage PSD because a small number of mortgage lenders do not submit data to the CML.

We publish other sources of mortgage data, such as those derived from the Mortgage Lending and Administration Return (MLAR) which may not be directly comparable to mortgage PSD due to differences in data coverage. For example, further mortgage advances are included in the MLAR but not in the PSD. Users of this report are therefore advised to bear these factors in mind when comparing mortgage PSD with other related data.

7. The overall trend in mortgage sales

Mortgage sales of 0.90m were reported between 1 April 2011 and 31 March 2012 (versus approximately 0.87m a year ago). Of all the lenders that reported mortgage sales using PSD, the top five accounted for about 64% of all sales by volume, the top ten for 86% and the top twenty for 94%. There has been an increase in market concentration among the top five and ten market providers with respect to last year. However, the market share remained fairly stable for the top twenty provider firms.

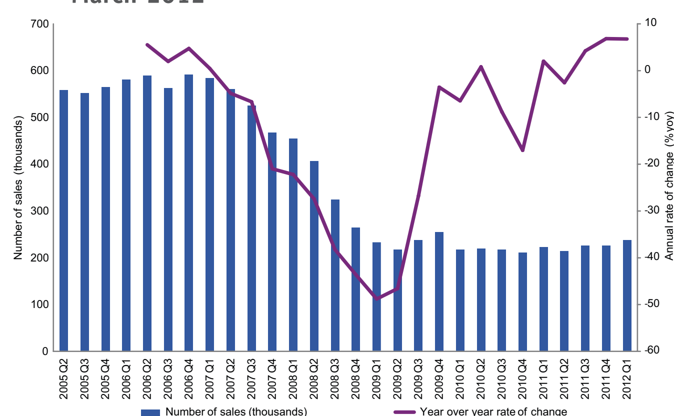
Between 1 April 2011 and 31 March 2012 (2011/12), mortgage sales rose 3.7% over the previous fiscal year. Following a decline in Q2 2011, the number of mortgages sold increased in Q3 2011, remained stable in Q4 2011, and rose by 5.1% qoq[2], s.a in Q1 2012. The increase in the final quarter may be attributable to the extension of the stamp duty holiday. The annual rate of change moved into positive territory in Q3 2011 and has remained there ever since, rising by 6.8% yoy in Q1 2012. However, this relatively robust figure is the statistical by-product of very low level of mortgage sales in Q1 2011 rather than an indicator of a meaningful recovery in the mortgage market.

1 See – www.census.gov/srd/www/x12a/

2 From now onwards, qoq stands for quarterly rate of change and yoy stands for annual rate of change (year over year).

Economic and financial developments during April 2011-March 2012 were unsupportive of the mortgage market. UK banks' exposures to European real economy and banking sector, as well as direct exposures to eurozone sovereigns, made them vulnerable to the euro area sovereign debt crisis. The intensification of the crisis raised funding costs for mortgage lenders, some of which were passed on to customers. The uncertain economic outlook, along with tight (and increasingly expensive) wholesale funding, have driven some financial institutions to tighten mortgage lending criteria.

Figure 1: Trend in mortgage sales – April 2005 to March 2012



Source: FSA Mortgage PSD. Notes: RHS stands for right hand side. Data are seasonally adjusted.

Table 1: Selected macroeconomic indicators

	RICS Survey, average sales per chartered surveyor*	UK Halifax, House Price Index: all houses: all buyers, % yoy	GfK Consumer Confidence Barometer, s.a., % balance	UK FTSE all share price index	GDP growth, % qoq	Unemployment rate	Availability of secured credit
2011 - Q1	14.7	-3.52%	-28	3068	0.46%	7.70%	2.8
2011 - Q2	14.7	-1.73%	-25	3097	-0.09%	7.90%	2.9
2011 - Q3	14.7	-0.57%	-30	2654	0.59%	8.30%	8.4
2011 - Q4	15.2	-2.30%	-33	2858	-0.36%	8.40%	1.9
2012 - Q1	15.5	0.80%	-31	3003	-0.32%	8.20%	3.8

Sources: Royal Institution of Chartered Surveyors (RICS), Halifax, GfK NOP, Financial Times, Office of National Statistics, BoE, Haver Analytics.
Note: *Completed sales per surveyor.

Table 1 illustrates that recent economic developments have not worked towards stimulating the mortgage market. Consumer confidence has deteriorated further between Q2 2011 and Q1 2012 (from -25 to -31); the unemployment rate has risen during the same period (from 7.9% to 8.2%); the economy re-entered recession in Q1 2012, and house prices recorded three consecutive contractions (between Q2-Q4 2011). In addition, real disposable income has been eroded by high inflation and low wage growth. The type of borrowers that have driven the surge in mortgage sales (first-time buyers), and the house price bands which have been affected the most (houses costing up to £250,000, see Section 8.1), indicate that the rise in mortgages sales since Q2 2011 has been driven by the stamp duty exemption.

The rise in mortgage sales has coincided with a significant increase in the number of (non-regulated) buy-to-let mortgages, which are not captured in PSD. According to the Council of Mortgage Lenders the volume of buy-to-let mortgages rose by 33% in 2011/12 versus 2010/11.[3] The FSA has flagged the possible misuse of buy-to-let mortgages (in place of residential mortgages) as an emerging risk.[4]

Number of provider and seller firms

All mortgage products in the market are created by what we refer to as 'provider firms', while selling firms are those which then sell these mortgage products. Selling firms can sell either a product they have created or one created by another firm. Thus, each transaction potentially has two firms attached to it; the seller and the provider. For direct sales, the seller and the provider will be the same firm; for intermediated sales, they will be different firms. Here we only count active[5] provider or selling firms. There are far more selling firms than provider firms. Since Q2 2005, there has been an average of 10,211 selling firms and 149 provider firms per quarter.

In the period 2011/12, in line with the observed increase in the number of mortgage sales, there has been a rise in both the number of selling firms (which rose by 0.8% to 7,706) and of provider firms (which rose by 10.4% to 137), although both remain well below their long-term average.

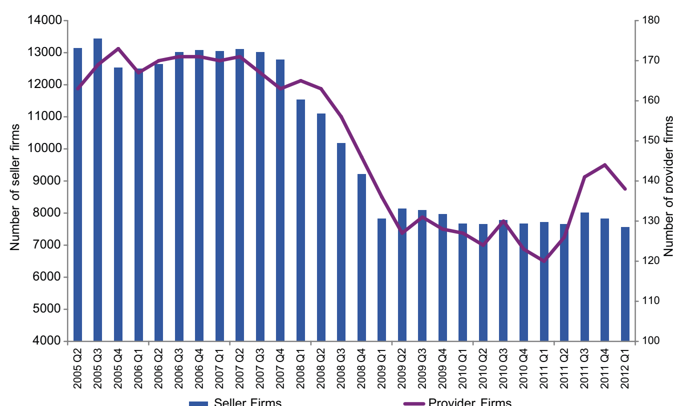
3 See CML Data (Buy to Let) – www.cml.org.uk/cml/media/press/3204)

4 See Retail Conduct Risk Outlook 2012 – www.fsa.gov.uk/static/pubs/other/rcro12.pdf

5 By 'active', we mean firms that have traded in the market, either providing or selling mortgages. Authorised firms that have not provided or sold any mortgage will not be accounted for.

There is a close correlation (95%[6]) between the number of provider firms and the number of selling firms in the market (see Figure 2). Having both reached high levels prior to the financial crisis, they experienced a substantial decline in 2008. Numbers remain below pre-crisis levels mainly due to mergers and acquisitions and because firms have been leaving the market.[7] For example, several non-deposit takers that were provider firms were unable to obtain funding to continue their mortgage business.

Figure 2: Number of mortgage providers and sellers – April 2005 to March 2012



Source: FSA Mortgage PSD

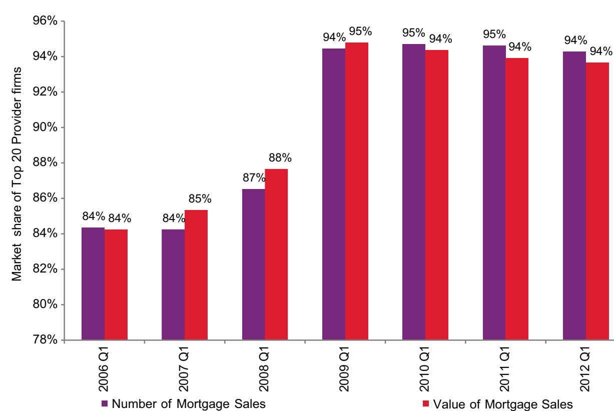
The number of selling firms has remained relatively stable between Q1 2010 and Q2 2011. However, in Q3 2011 there was an increase, followed by two successive quarters of decline, reaching an all-time low of 7,560 in Q1 2012.

Market share of top providers

The evolution of market shares (both in terms of number of mortgages sold and in terms of the value of mortgages) illustrates a trend towards consolidation. As explained above and in our previous edition of Mortgages PSD Trends Report[8], the mergers and acquisitions (and cancellations) of mortgage lenders, especially in Q4 2008 and in 2009, have translated into an increase in the degree of concentration (here measured as the market share of the top twenty provider firms at any point in time).

Since 2009, the degree of concentration (among the top twenty provider firms) has remained broadly stable – especially in terms of sales volumes. There has, however, been a modest decrease in both market shares (volume and value of sales) in Q1 2012 versus Q1 2011. The reduction is more apparent for the top five provider firms which declined from 65% to 60% (for mortgage sales) and from 64% to 60% (for value of mortgages).

Figure 3: Top 20 mortgage provider firms – market share in Q1 of each year



Source: FSA Mortgage PSD

Type of firms

We now look at the evolution of mortgage sales over time, across types of provider firms. We differentiate between six categories: a) banks; b) subsidiaries of banks; c) building societies; d) subsidiaries of building societies; e) non-banks; and f) other lender types.[9] This breakdown is consistent with the categories in the MMR Data Pack, Supplement to CP11/31.[10]

6 This is the correlation coefficient between both series.

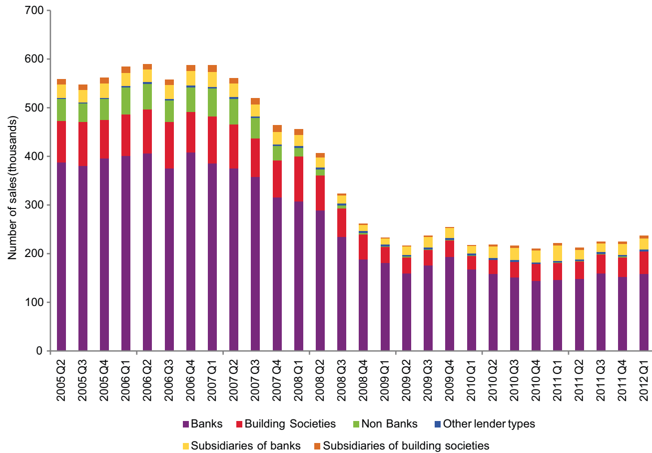
7 We have recorded 18 major mergers or acquisitions since the beginning of the sample, several of them in 2008 and 2010.

8 See – www.fsa.gov.uk/pubs/other/psd_mortgages_05_11.pdf

9 Non-banks is an illustrative category that identifies lenders with no deposit-taking permissions that targeted specialist markets and are independent of the UK retail banks and building societies. This means that lenders which are subsidiaries of foreign investment banks are classified as 'non-banks'. Some lenders may have shifted category during the period (2005-2011). In such cases, where possible, the type was assigned as it was before 2008.

10 See MMR Report – www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf

Figure 4: Mortgage sales across types of provider firms over time



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

The majority of mortgages are provided by banks (almost 69% in 2011/12), followed by building societies (18% over the same period). Banks and subsidiaries of banks have lost market share since previous fiscal year (by 0.6 and 2.8 percentage points respectively). The main beneficiaries have been building societies, which gained three percentage points.

Mortgage sales expanded the most for non-banks (by 131%) albeit from a very low base, followed by building societies (24.5%). Not surprisingly, they contracted for subsidiaries of banks (by 20%).

8. The characteristics of new mortgage sales

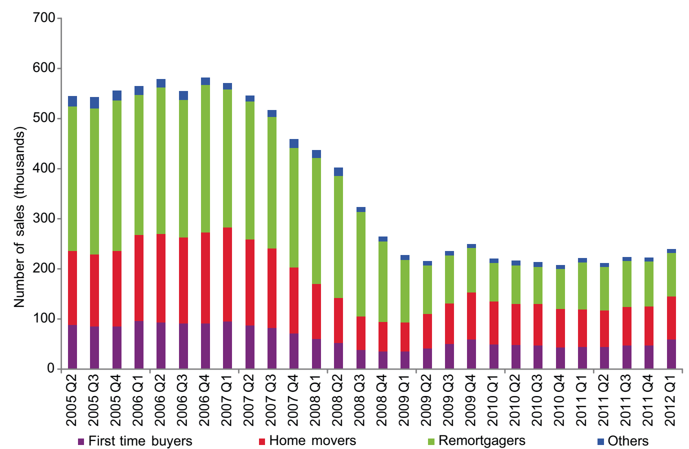
8.1 Borrower type – number of sales

The increase in new mortgage purchases in 2011/12 has been driven by remortgagers (which expanded by 9.8% versus 2010/11) and first-time buyers (which grew by 6.7% versus 2010/11). However, new mortgage sales to home movers have declined by 1.9%. The so-called 'second steppers', those that have made the first step into home ownership some years ago, are now finding it difficult to move up the property ladder because of constraints on income and housing equity.[11] They may be trapped because their financial circumstances or the lender's affordability criteria have changed (becoming so-called 'mortgage prisoners[12]'). We estimate that nearly half of those borrowers who have taken out a mortgage since 2005 could have difficulty remortgaging[13] – although it is important to recognise that there is no standard approach to defining 'mortgage prisoners'.

Mortgages sales to right-to-buy customers, a type of borrower that could be considered potentially risky[14], recorded a substantial contraction (by 13.3%).

With respect to the previous year, remortgagers have gained relevance (accounting for 39% of new mortgages versus 37% the previous period). In contrast, the proportion of new mortgage sales to home-movers declined to 35% from 37%. For first-time buyers it has increased only slightly to 22% from 21%.

Figure 5: Mortgage sales by borrower type – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

The increase in mortgage sales by first-time buyers may reflect a desire to purchase in order to benefit

11 See CML Annual report 2011 – www.cml.org.uk/cml/filegrab/7cml-annual-report-2011.pdf?ref=8252

12 See MMR Report – www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf, page 31.

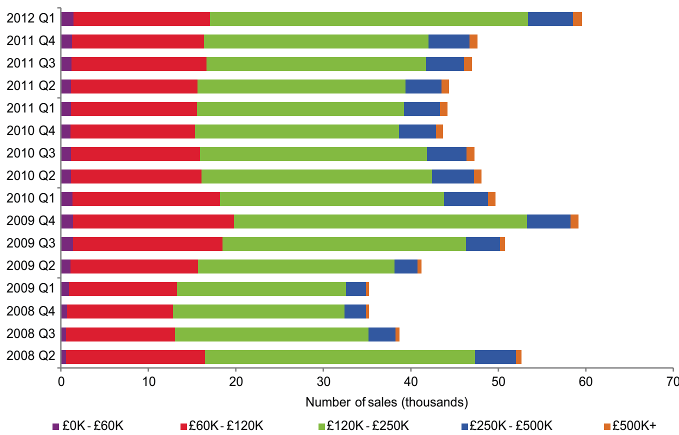
13 See MMR Report – www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf, page 31.

14 See MMR – www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf, page 146.

from the stamp duty exemption on properties up to £250,000. The concession ended in March 2012. Other schemes aimed at first-time buyers such as Firstbuy[15], which was launched in September 2011, may also have helped increase sales during this period.

Interestingly, mortgage sales to first-time buyers of properties between £120,000 and £250,000 expanded the most, by 53.1% (s.a.) between Q2 2011 and Q1 2012. This compares with a contraction of 10% (s.a.) the previous year (Q2 2010 to Q1 2011), suggesting that the end of the stamp duty exemption is behind the increase in mortgage sales.[16]

Figure 6: First-time buyers: Number of sales by property value bands

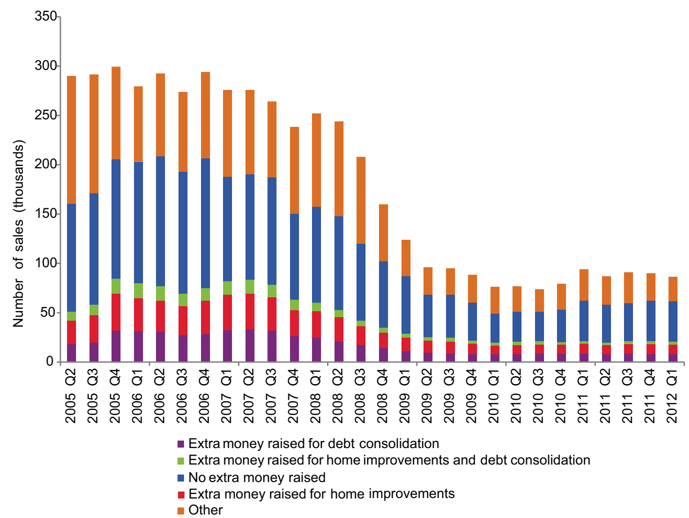


Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

There is not a significant difference between volume and value trends across type of borrowers, with more pronounced expansions in volume terms for first-time buyers and remortgagers. As a result, the average mortgage values for both types of borrowers increased rapidly in 2011/12 versus 2010/11.

8.2 Remortgage purpose

Figure 7: Remortgage sales by purpose of loans



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

There are two main types of remortgagers: those who withdraw equity and those who do not. The latter is represented here as 'no extra money raised', while in the first category we differentiate between those who raise extra money for home improvements, for debt consolidation, or for a combination of both. Remortgaging with 'no extra money raised' has become more popular in 2011/12, consistent with the observed trend towards deleveraging. According to the ONS, household debt over GDP has declined from 103.6% in Q4 2010 to 100.6% in Q4 2011. Sales of mortgages with no extra money raised have expanded significantly by 18.7% with respect to 2010/11. In contrast, new mortgage sales with extra money raised for a combination of debt consolidation and home improvements (possibly the most risky category) and debt consolidation, both declined, by 3.5% and 5.3% respectively, in the same period (see Figure 7).

Since mid-2007, there has been a sustained decline in the sales of mortgages that allow for equity withdrawal. Mortgage lenders seem less inclined towards lending in weak economic conditions and as funding remains tight. Additionally, they have become better at pricing

15 The measure was announced in the 2011 budget. The scheme allows first-time buyers to purchase a newly built property using a 5% deposit, with a further 20% deposit provided in the form of a five-year interest-free loan jointly funded by the developer and the government.

16 The exemption started on 24 March 2010 and ended two years later, on 24 March 2012.

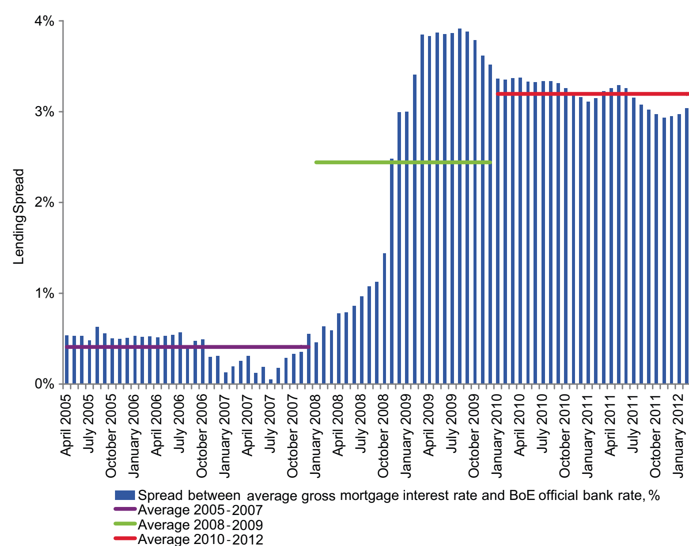
risks. There also seems to be a genuine interest from borrowers to pay down their debts, especially in the context of ongoing economic uncertainty and tight credit conditions. In fact, according to the research by Barclays, 10% of homeowners were overpaying on their mortgage payments in March 2011, and the expectation was for this proportion to rise.[17]

8.3 Lending spreads

Mortgage spreads (calculated as the difference between mortgage rates and the Bank of England base rate) declined in 2011/12 to 3.09% from 3.26% in 2010/11. They fell from April 2011, reaching their lowest point in November 2011 at 2.93% and have increased since then. Wholesale funding market disruptions have spilled over into the retail funding market, increasing competition and pushing up retail funding costs gradually. The recent rise reflects the deterioration in the longer term wholesale funding markets due to the eurozone crisis, as well as uncertainty over the impact of impending regulatory changes and the economic outlook in the UK.[18] Indeed, wholesale debt issuance continues to be very weak, and mostly secured. In this context of strong funding competition, retail margins of UK banks remain compressed.[19]

Spreads are still relatively high by historical standards (see Figure 8), although below the levels reached at the height of the financial crisis in 2009. Renewed tensions in the inter-bank lending market raised the spread in March 2012 to 3.15%, the highest level since July 2011. Note that lending spreads are not necessarily an indication of lending margins; these would largely depend on operating and funding costs, which are volatile and uncertain in the current economic climate.

Figure 8: Mortgage spreads over time – April 2005 to March 2012



Source: FSA Mortgage PSD, BoE.

Tight margins on new lending will be partially offset by rising standard variable rates (see Figure 10). However, this could increase the risk of default for heavily indebted households.

8.4 Types of interest rate[20]

Sales of fixed-rate mortgages continued to expand in 2011/12 (by 24.2%, compared with the previous year). As a result, they accounted for 62.5% of sales in 2011/12, ten percentage points more than in 2010/11. In contrast, sales of mortgages linked to variable rates declined significantly; by 27.6% for standard variable, 21.6% for tracker, and by 19.3% for capped rates. The number of mortgage sales linked to discounted variable rates remained broadly stable.

Despite the continuous sales of fixed-rate mortgages, most existing borrowers are on floating rates and thus vulnerable to interest rate hikes. Although expectations are for the base rate to remain unchanged in the immediate future, disruptions in the wholesale market are already affecting retail mortgage rates. According to the latest Mortgage Lenders and Administrators Return (MLAR), although 55% of regulated new mortgages in Q1 2012 were taken out

17 See www.mortgagestrategy.co.uk/economy/just-10-of-homeowners-overpaying-on-their-mortgage/1027793.article

18 See *Trends in Lending* – July 2011', Bank of England

19 See *Retail Conduct Risk Outlook 2012* – www.fsa.gov.uk/static/pubs/other/rcro12.pdf

20 PSD Interest Rates are optional for reporting with approximately 68% of transactions having an initial interest rate figure attached.

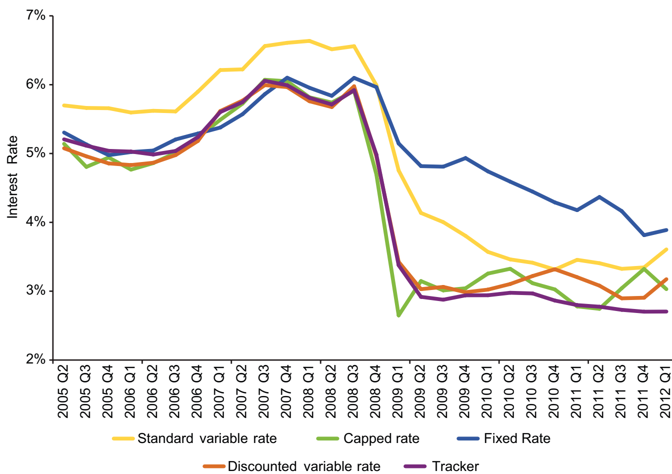
with fixed rates, only 28% of balances outstanding are linked to fixed rates.[21]

After fixed-term mortgages, the two most popular options are tracker mortgages (which now represent 23.2% of total sales, down from 30.7% in 2010/11), followed by discounted variable (which account for 7.8%, down from 8% the previous year).

This increase in sales of mortgages linked to fixed rates is partly due to the competitive market; with fixed rate initial mortgage rates declining 48bp from 4.4% in Q2 2011 to 3.9% in Q1 2012 (see Figure 9). In addition, consumers may also feel more comfortable with this type of mortgage for security reasons at a time of high uncertainty, and they are more eager to lock in deals in anticipation of higher (if not imminent) future rates.

There seems to be demand in the UK for mortgages linked to fixed rates for a prolonged period of time, such as 30-year fixed contracts.[22] There are currently no mortgages with guaranteed lifelong interest rates; there are, however, mortgage lenders offering 10-year fixed mortgages.[23]

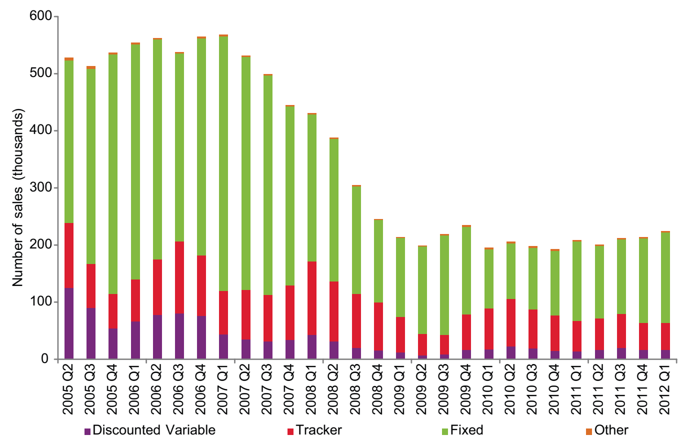
Figure 9: Interest rate type by initial interest rate – April 2005 to March 2012



Source: FSA Mortgage PSD

In comparative terms, initial standard variable rates rose from 3.4% in Q2 2011 to 3.6% in Q1 2012, and capped rates from 2.7% to 3.0% – partially explaining the decline in mortgage sales for these types of mortgages. It is also expected that these rates may increase further in light of the difficulties providers face in securing long-term wholesale funding[24], rendering fixed-term rates even more attractive. The remaining types of rates did not change by more than 10bp during this period.

Figure 10: Mortgage sales by type of interest rate – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

It should be noted that, although mortgage rates still remain less differentiated than in the pre-crisis period, the dispersion is significantly lower than in 2009 when they reached 2.5%. Indeed, the difference has been declining ever since, and it is now at 1.2% (see Figure 9).

8.5. Repayment method

Another trend is the move away from interest-only products towards less risky (e.g. capital and interest) repayment methods. Indeed, sales of new mortgages with capital and interest repayment methods have expanded by 10.9% in 2011/12 with respect to the previous fiscal year. This compares with a contraction of 17.5% for interest-only mortgages.[25] Equally, the proportion of interest-only mortgages with an

21 See Table 1.22 in Part II of www.fsa.gov.uk/Pages/Library/Other_publications/statistics/index.shtml

22 See www.communities.gov.uk/newsstories/housing/20034681

23 Norwich and Peterborough Building Society launched a 10-year fixed-rate mortgage in January 2012.

24 See *Trends in Lending* – April 2012, Bank of England.

25 Including interest only mortgages with known repayment vehicles (ISAs, endowments and pensions) and unknown repayment methods.

unknown repayment vehicle has continued to decline and is now hovering around 11% in Q1 2012, down from 26% in late 2007. These developments partly reflect increased conservatism in the wake of the US mortgage-backed securities crisis, driving both lenders and borrowers away from lending that relies heavily on equity gains. In addition, several major UK banks have tightened their lending criteria on interest-only mortgage products during the period under study.

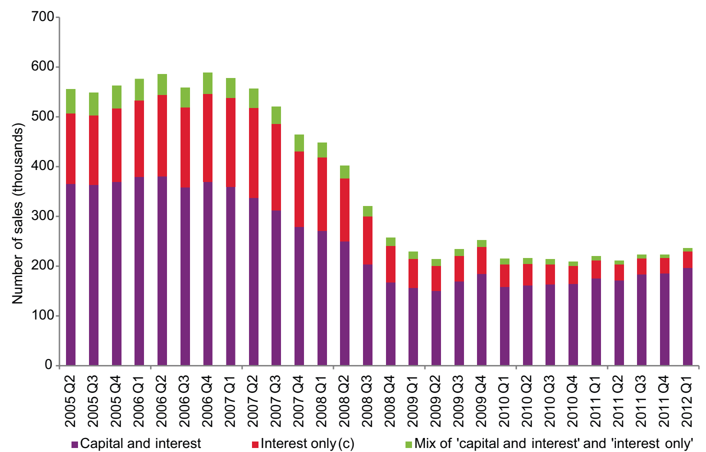
PSD also allows us to examine how the repayment method varies according to the purpose of the loan. Table 2 shows that the capital and interest repayment method is particularly popular among right-to-buy buyers and first-time buyers (for both, 96% of borrowers chose this method). The ratios have increased with respect to last year (when they represented 92% and 89% respectively). It is unclear whether this represents the preference of first time buyers or whether lenders are reluctant to offer mortgages with different characteristics. Few borrowers go for interest-only mortgages with an unknown repayment method, the highest proportion being for remortgagers and home movers who have lower LTV needs than first-time buyers. With respect to the last fiscal year, the proportion has declined across all type of borrowers except remortgagers.

Table 2: Mortgage sales by repayment method and type of borrower – April 2011 to March 2012

	Capital and interest	Interestonly with an unknown repayment vehicle	Interest only with a repayment vehicle	Mix of 'capital and interest' and 'interest only'	Unknown repayment method
Total	736,249	100,937	28,789	26,815	6,979
Remortgagers	76%	15%	4%	4%	0%
Home Movers	82%	12%	3%	3%	0%
First-Time Buyer	96%	3%	1%	0%	0%
Right To Buy	96%	1%	2%	0%	0%
Other	52%	22%	2%	1%	22%

Source: FSA Mortgage PSD.

Figure 11: Mortgage sales by repayment method – April 2005 to March 2012



Source: FSA Mortgage PSD. Notes: Data have been seasonally adjusted.
* Includes interest only mortgages with and without repayment vehicles.

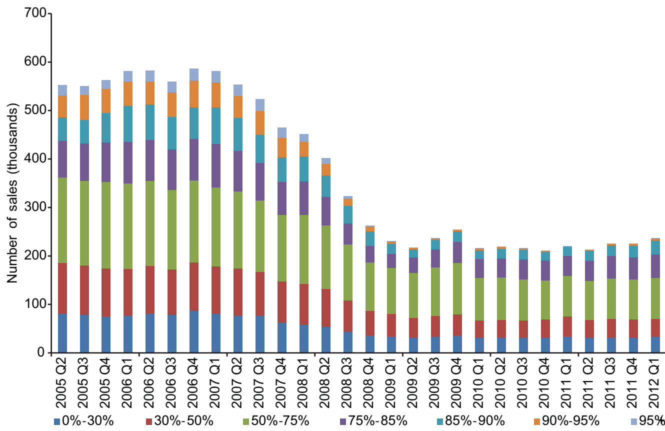
8.6 Loan to values (LTV) ratios

Figure 12 shows the evolution of mortgage sales by loan–to-value ratios (LTV). The rise in mortgage sales has been concentrated in the 75%+ LTV bands, with marked increases in the 85%-90% and 90%-95% bands, albeit from a very low base. In 2011/12, these expanded by 21.8% and 23.3% respectively compared with 2010/11. The concentration of sales in the high LTV bands is due to the role played by first-time buyers, who have driven the rise in the last few quarters with the aid of the government's stamp duty land tax relief scheme. They need higher LTV ratios and income multiples (see section 8.10) than other borrower types to enter the property market. As a result, the average LTV has increased slightly from 59% in Q2 2011 to 61% in Q1 2012.

There was also an increase in the number of mortgages sold within the 95%+ band (by 5%); however this segment represented only 0.2% of sales in 2011/12. Mortgage sales below the 75% LTV band declined by 0.9% in 2011/12 on an annual basis. As regards LTV bands, mortgage lenders are not acting in a more conservative manner with respect to last year.

The most popular band continues to be 50%-75%, which accounted for 37% of all sales during the fiscal year.

Figure 12: Mortgage sales by loan-to-value ratios – April 2005 to March 2012



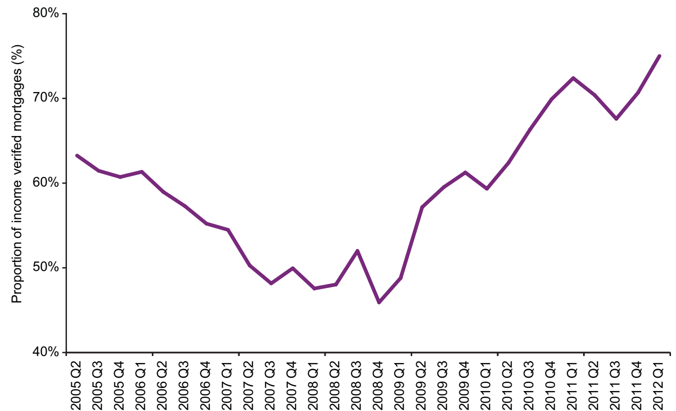
Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

8.7 Income verification and risk-based lending

The FSA's July 2010 MMR Consultation Paper on responsible lending[26] outlined particular concerns around mortgage affordability where income had not been verified. As illustrated in Figure 13, post-crisis, there has been an increase in the proportion of income-verified mortgages. This trend has continued in recent quarters, with the ratio at an all-time high of 74% in Q1 2012 versus 46% in Q4 2008. Overall, during 2011/12 the number of income-verified mortgages grew by 8.6% with respect to 2010/11, while sales of non-verified mortgages declined by 6.4% in the same period.

The increasing difficulties in obtaining credit and the rising costs of borrowing may have driven financial institutions towards more stringent income verification processes.

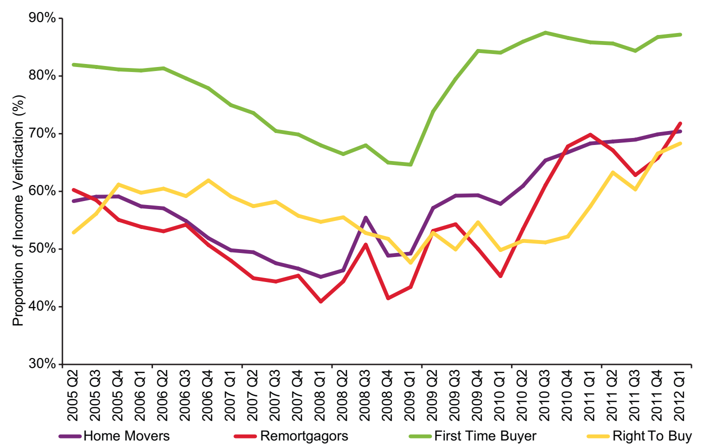
Figure 13: Overall Income verification – April 2005 to March 2012



Source: FSA Mortgage PSD.

Income verification for lower risk borrower types, such as remortgagers and home-movers, is currently (as of Q1 2012) at 70% and 72% respectively. However, verification in the higher risk first-time buyer market is significantly higher at 87%, indicating that financial institutions are taking a risk-based approach to income verification (see Table 3). The type of borrower where the proportion has increased the fastest between Q2 2011 and Q1 2012 – by 5 percentage points – is right-to-buy. Note that they present the lowest proportion across known borrower types (and are considered relatively risky).

Figure 14: Income verification by borrower type – April 2005 to March 2012



Source: FSA Mortgage PSD.

26 CP10/16 – www.fsa.gov.uk/pubs/cp/cp10_16.pdf

Table 3: Proportion of income verified mortgages by borrower type – Q1 2011 to Q1 2012

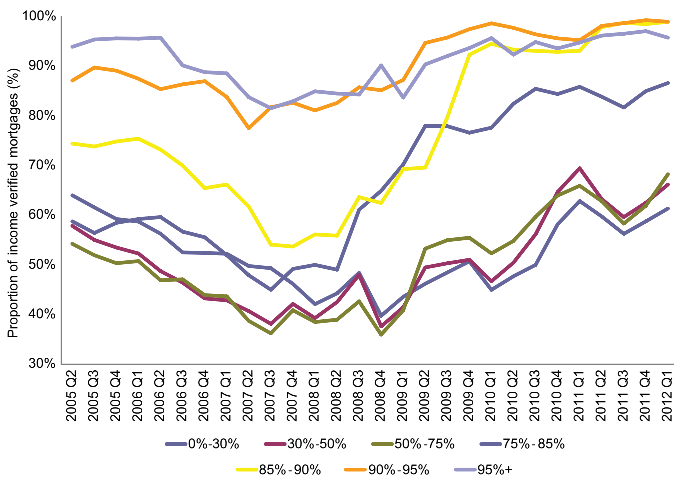
	2011 Q2	2011 Q3	2011 Q4	2012 Q1
Home Movers	69%	69%	70%	70%
Remortgagors	67%	63%	66%	72%
First-Time Buyer	86%	84%	87%	87%
Not Known	52%	56%	61%	55%
Right To Buy	63%	60%	67%	68%
Other	40%	37%	35%	34%

Source: FSA Mortgage PSD.

Mortgages with lower LTV ratios (<75%) are subject to significantly lower levels of income verification when compared to higher LTV bands (see Figure 15). Once we cross the 85% threshold, the proportion of income-verified mortgages is above 96%.[27] The 90%-95% LTV band recorded the highest income verification rate in 2011/12 at 99%. At the other extreme, we have the income verification rate for the 0%-30% LTV band, which was 59%.[28] This is again indicative of financial institutions taking a risk-based approach towards mortgage lending.

With the exception of the lowest 0%-30% LTV band, all of the others experienced an increase in the proportion of income-verified mortgages in 2011/12 versus the previous fiscal year.

Figure 15: Income verification by LTV ratio – April 2005 to March 2012

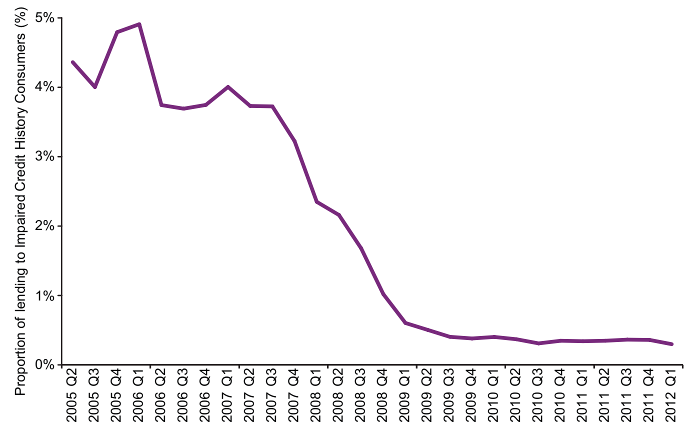


Source: FSA Mortgage PSD.

8.8 Mortgages to borrowers with impaired credit history

Mortgage sales to consumers with impaired credit history have continued to decline. In Q1 2012 they represented only 0.29% of new mortgages versus 0.34% in Q2 2011. During the peak of the mortgage market in 2006, they reached their historical maximum of 4.8%. The proportion has declined consistently ever since, with the most dramatic adjustment occurring before 2010. Admittedly, this is a niche market, which only accounts for 3,111 of new mortgage sales in 2011/12 versus 897,806 for borrowers without an impaired credit history.

Figure 16: Sales to borrowers with impaired credit history– April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

8.9 Income multiples

During 2011/12, sales of mortgages have increased in the higher income multiples area. Income multiples of 5.5x have seen a rise of 24% versus the last fiscal year, while those between 4.5-5.49x experienced a 12% expansion. As with the higher LTV ratios, this is partly due to the role played by first-time buyers in driving mortgages sales, since they need to stretch their finances in order to enter the property market. Sales for lower income multiples increased only slightly during this period (between 2% and 3%). Not surprisingly, the average income multiple has risen from 2.90x in Q2 2011 to 3.00x in Q1 2012 (see Figure 17).

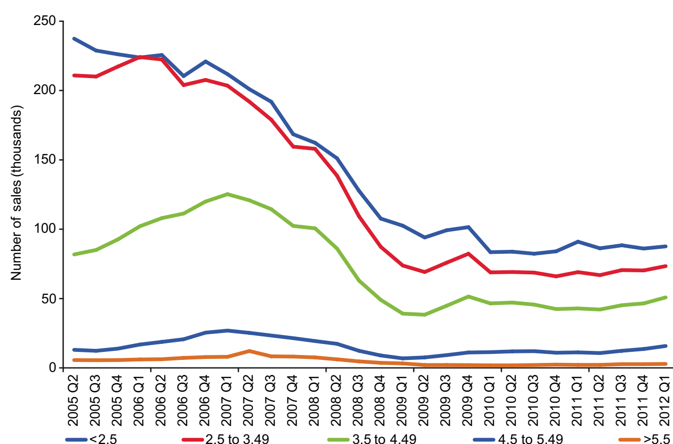
The most popular income bracket in 2011/12 was still the lowest (<2.5x), representing 40% of total mortgage

27 Following Basel II, there is an incentive for banks and building societies to reduce their average LTV ratio because of capital requirements for loans with LTV ratios greater than 80%.

28 This band could also include retention business where the income has previously been verified.

sales, followed by 2.5x to 3.49x, which accounted for 32%, and 3.5x to 4.49x , which accounted for 21% of sales.

Figure 17: Average income multiples over time



Source: FSA Mortgage PSD. Data have been seasonally adjusted.

8.10 Lifetime mortgages

Lifetime mortgages are a regulated mortgage contract, which is targeted at older customers and is repaid by selling the property when the customer dies, goes into long-term care or otherwise vacates the property. The number of lifetime mortgages sold in 2011/12 has expanded by 4.7% from the previous year. This is above the expansion rate of non-lifetime mortgages. As a result, the proportion of this type of mortgage has increased slightly during the period under study, reaching 2.1% in Q2 2012.

There are different reasons why borrowers may want to buy lifetime mortgages (demographics, life choice). The jump in the proportion of lifetime mortgages soon after the crisis suggests that economic factors are also at play. Some people of a certain age may not have any other option if they cannot afford to live off their pension – especially at times when economic activity is contracting.

Customers between 66 to 75 years of age accounted for 51.8% of lifetime mortgages in 2011/12, followed by the 56 to 65 years band (25.8%), and 76+ (21.8%).

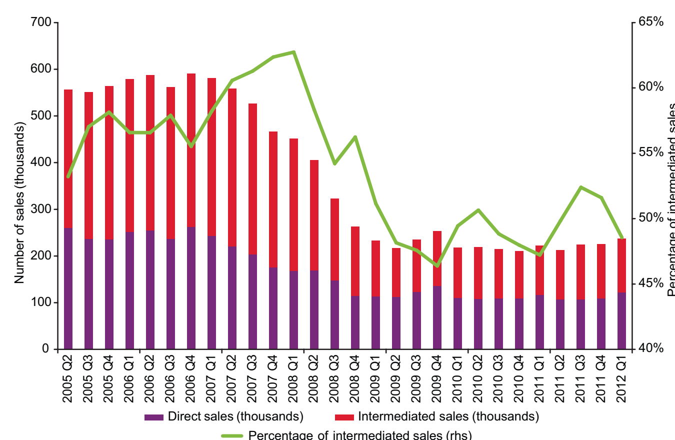
8.11 Sales channels

Intermediaries have been good at keeping their market share throughout the last fiscal year. Mortgage sales through intermediaries expanded by 8.0% in 2011/12 versus 2010/11, while they remained broadly unchanged for firms selling directly to customers.[29] However, since Q3 2011, there has been a clear decline in the proportion of intermediated sales in the mortgage market (from 52.4% (s.a) to 48.6% (s.a.) in Q1 2012).

Since intermediaries are more likely to provide advice, we would expect an increase in the number of advised mortgage sales in the year.

Prior to the crisis, most mortgage sales were made via intermediaries (as many as 64% in Q1 2008). This changed in H2 2008, when the proportion started to decline. Since then the rate has lingered between 56% and 46%.

Figure 18: Mortgages sales by channel – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

According to Moneyfacts, the number of mortgage products available to UK mortgage intermediaries has risen by 421 between Q2 2011 and Q1 2012 to 2,991.[30] The increase in the number of products may have benefitted intermediaries more than providers selling directly to borrowers since it widens the range of options available to them.

8.12 Advised sales

Customers of new mortgages typically receive advice when buying these products. The trend has been for an increase in the relative importance of advised sales. This tendency continued in 2011/12, with the number of advised mortgage sales increasing by 7% versus 2010/11, while non-advised sales declined by 4%. As a result, the proportion of advised sales reached 74% between March 2011 and April 2012 (versus 72% the previous year). This is consistent with the findings of

29 A sale where the provider firm and the selling firm is the same is considered a direct sale. In other words, the product is sold to the customer directly by the provider. See appendix at the end of the document.

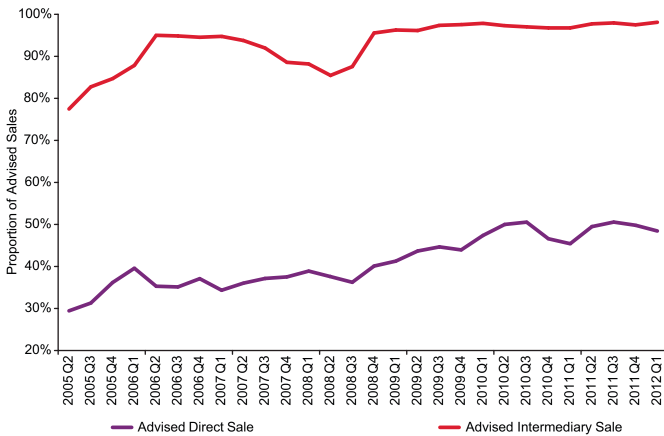
30 See http://moneyfacts.co.uk

Section 8.12, where we recorded a better performance for intermediaries than for firms selling directly to the public. As can be seen in Figure 19, the proportion of advised sales for intermediaries is significantly higher (98% versus 48% for direct sales in Q1 2012).

Advice is a major part of the offering provided by mortgage intermediaries. This service may have attracted more customers and led to an increase in market share. In contrast, approximately 50% of direct mortgage sales are advised.

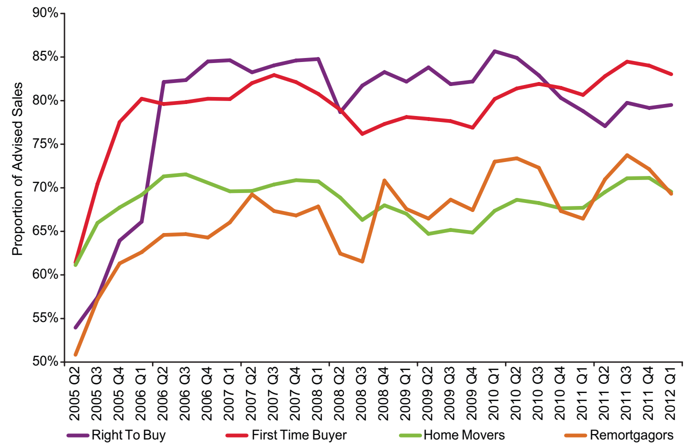
As can be seen in Figure 20, the proportion of advised sales for right to buy borrowers and first-time buyers is significantly higher than for home movers and remortgagors.

Figure 19: Mortgages sales by channel – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

Figure 20: Advised sales by borrower type – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

9. A closer look at first-time buyers

Possibly the most interesting category of borrowers is first-time buyers. The flow of new buyers is critical to the overall health of the market. However, they tend to come under particular stress during recessions, since unemployment is also highest among the youngest. In Q2 2011, the unemployment rate for people of 50 years of age or older was 4.8% versus 20% for those between 18 to 24 years.

There have been some pressures on mortgage lenders to make more funding available to new customers. In November 2011, the government published *Laying the foundations, a housing strategy for England* which, among other objectives, aimed to improve access to home-ownership for two groups: first-time buyers and military personnel.

The main barrier to entry into the housing market for first-time buyers is saving up for a deposit following the rise in house prices. Indeed, the average housing deposit has increased significantly since 1990.[31] There is anecdotal evidence suggesting that potential borrowers feel rather pessimistic about the application process, which may prevent them from even applying.[32] In order to support first-time buyers during the economic downturn, the UK government introduced a two-year scheme whereby first-time buyers would receive stamp duty land tax relief for residential property purchases up to £250,000. The measure was extended until 24 March 2012.

31 According to Mortgage Introducer, the average housing deposit has risen from £6,793 to £65,924 in 2011. See www.mortgagestrategy.co.uk/housing-market/house-deposits-increase-tenfold-in-20-years/1038007.article

32 See www.mortgagestrategy.co.uk/distribution/two-thirds-of-20-to-45-year-olds-have-given-up-on-home-ownership/1031873.article

During the last fiscal year the industry has launched an array of new products specifically aimed at first-time buyers. These include mortgage products with high LTV ratios (up to 100%[33]), lower (or no) deposits, and schemes to help them save towards their deposits.

First-time buyers and type of interest rates

Table 4 shows that 79% of first-time buyers opted for fixed-rate mortgages in 2011/12; an increase of 15 percentage points with respect to 2010/11. The preference towards fixed-rate mortgages has occurred at the expense of tracker deals, which represented only 15% of new mortgage sales in 2011/12 versus 26% in the previous year.

First-time buyers and repayment type

96% of first-time buyers have taken out traditional capital and interest loans, up 4 percentage points with respect to the previous year (see Table 5). This is in line with overall market trends, which have shown an overall increase in the proportion of both fixed-rate and capital and interest repaying borrowers.

Table 4: Mortgage sales by type of borrower and type of interest rate type – April 2011 to March 2012

	Remortgagors	Home Movers	First-Time Buyer	Right To Buy	Other
Total	354,501	315,309	197,261	2,647	30,051
Fixed-Rate	60%	56%	79%	81%	53%
Tracker	27%	25%	15%	16%	12%
Discounted variable rate	8%	9%	5%	1%	2%
Standard variable rate	4%	9%	1%	1%	10%
Capped rate	1%	0%	0%	1%	0%
Other	0%	0%	0%	0%	22%

Source: FSA Mortgage PSD.

Table 5: Mortgage sales by type of borrower and repayment type – April 2011 to March 2012

	Remortgagors	Home Movers	First-Time Buyer	Right To Buy	Other
Total	354,414	315,180	197,246	2,643	23,307
Capital and interest	76%	82%	96%	96%	66%
Mix of 'capital and interest' and 'interest only'	4%	3%	0%	0%	2%
Interest only	19%	15%	3%	3%	32%

Source: FSA Mortgage PSD.

First-time buyers and type of income

First-time buyers are more likely to take a sole income than a joint income mortgage. Around 54% of them take a sole income mortgage, a proportion that has remained relatively stable in the last four quarters. The Council of Mortgage Lenders points out that there has been an increase in the proportion of first-time buyers who receive assistance when entering the mortgage market since 2005. We do not know whether the first-time buyers captured by the PSD have been aided by friends or family, but we can see an increase in the average age of first-time buyers.

We do, however, have evidence from the PSD that first-time buyers require a higher income multiple to enter the marketplace. The estimated income multiple for first-time buyers (using a weighted average) was 3.31x in Q1 2012 compared to 3x for all borrower types. The overall income multiple has increased by 3.6%, which can be attributed to the increase in first-time buyers entering the market, in order to take advantage of the stamp duty exemption scheme.

First-time buyers and age bands

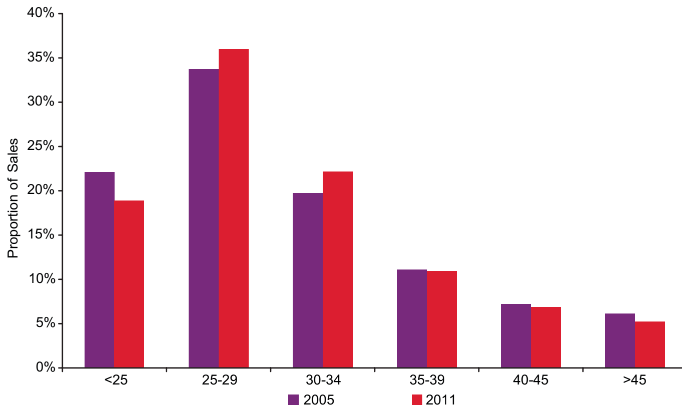
Figure 21 shows the proportion of first-time buyers by age group in 2011 and 2005. Most first-time buyers sit in the 25 to 29 years age band (36%), followed by the 30 to 34 years band (22%). Since 2005, the trend has been for a lower proportion of sales to under-25 years, and an increase to buyers in the 25 to 29 years and 30 to 34 years age bands.

33 According to Mortgage Strategy, there were three providers offering 13 products which involve 100% LTV as of August 2011. See www.mortgagestrategy.co.uk/concern-over-number-of-100-ltv-deals-without-guarantees/1036261.article

First-time buyers and LTV ratio

Not surprisingly, first-time buyers need higher LTV ratios than other types of borrowers; the average LTV ratio for first-time buyers in 2011/12 was 74% versus 60% for all borrower types. This can be better appreciated by comparing Figure 22 with Figure 12. For first-time buyers, the proportion of new mortgages with a LTV ratio of 75% or above is significantly higher (62% versus 32% for all borrower types).

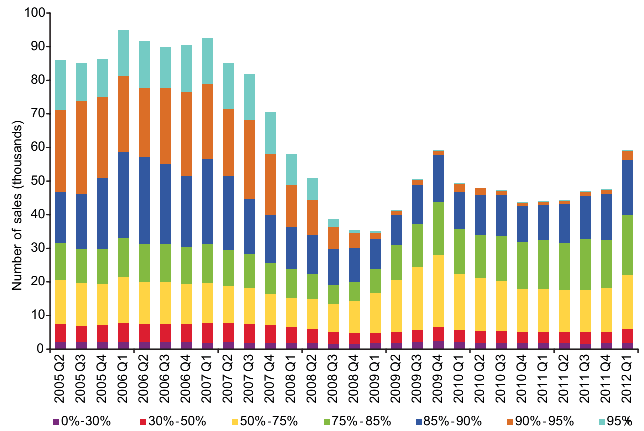
Figure 21: First-time buyers by age bands



Source: FSA Mortgage PSD.

Mortgages to first-time buyers show similar trends to those observed for other types of buyer. The LTV band that experienced the fastest growth was 95%+, which grew by 22 percentage points -although they only represent 0.4% of the first time buyers market – while those below 75% contracted by 4.2 percentage points.

Figure 22: First-time buyer mortgage sales by loan-to-value ratios – April 2005 to March 2012



Source: FSA Mortgage PSD. Note: Data have been seasonally adjusted.

10. Regional analysis

Information on new mortgage deals can be disaggregated by postcode areas across the UK. In every region, the number of new mortgages sold during 2011/12 was higher than in 2010/11. The largest rise was recorded in the north east (5.4%), while the smallest occurred in Northern Ireland (1.5%).

The north-south divide is also apparent when we look at the number of new mortgages sold normalised by regional population. Borrowers in the north are more likely to have mortgage arrears and be in negative equity than borrowers in the south.[34] Research from Standard and Poor's confirms that homeowners in the north are finding it more difficult to keep up with their mortgage repayments than those in the south.[35] This is consistent with our figures for the number of mortgage sales per 1,000 inhabitants across the different regions. The lowest ratio, at 9.8 mortgages per 1,000 inhabitants was recorded in Northern Ireland, while the highest, at 21.9, was recorded in the south west.

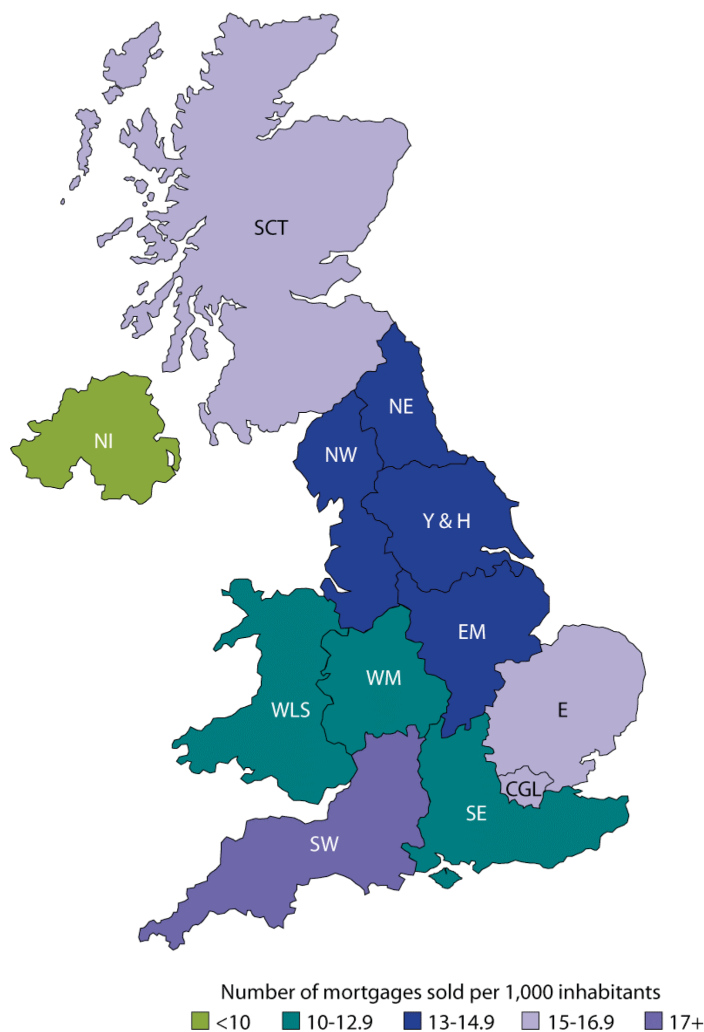
The evolution of housing prices in the last few quarters has contributed to perpetuate this difference; house prices in the north contracted significantly in several regions between Q2 2011 and Q1 2012 (by 11.8% in Northern Ireland and by 11.3% in Scotland); while they even increased slightly in the

34 See *Mortgage Finance Gazette* from 11 October 2011, www.mortgagefinancegazette.com/arrears/the-north-south-divide-widens/ and www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf page 35.

35 *Mortgage Finance Gazette* 11/10/2011

south (by 2.1% in Greater London and by 2.5% in the south east). This should have generated a higher number of negative equity and/or trapped borrowers in the northern regions. Borrowers who took out high LTV interest-only mortgages at the peak of the market are particularly affected.[36]

Figure 23: Ratio of mortgages to the UK regional population – April 2009 to March 2010



Sources: FSA Mortgage PSD and Office of National Statistics.

11. Appendix

PSD definitions[37] – mortgages[38]

Advised/non-advised sales — An advised sale occurs when an advisor of a regulated firm gives a personal recommendation to the customer after assessing the customer's needs and circumstances. This is specific and individual advice to the customer and is not generic.

A non-advised sale occurs when no personal recommendation is made to the customer. The customer receives information on the product to enable them to make an informed decision about whether it meets their own needs and circumstances. Non-advised sales include 'execution only' and 'direct offer transactions'.

Capped and collared — A variable interest rate that is guaranteed not to exceed a stated maximum rate (the capped rate) for a specific period of time. Also includes products where the interest rate is subject to a minimum rate (the collared rate).

Discounted rate — Where a discount is applied to the lender's standard variable rate, usually for a limited period.

Fixed-rate — Where the interest rate is fixed for a stated period.

Home reversion plan — An equity release arrangement where the occupier of a property sells the property (or a part interest in it) to the reversion provider and receives a lump sum and/or an income in return. The occupier retains the right to live in the property under a lease of life or until a specified event occurs.

Lifetime mortgage — A regulated mortgage contract, which is targeted at older customers and is repaid by selling the property when the customer dies, goes into long-term care or otherwise vacates the property.

36 See MMR – www.fsa.gov.uk/static/pubs/cp/mmr-datapack2011.pdf, page 34.

37 The definitions in this appendix have been compiled from various sources including the FSA Handbook Glossary, FSA Policy, Supervision Manual, Chapter 16 Annex 20G and the Council of Mortgage Lenders Housing Finance Issue, July 2005 and November 2006.

38 Mortgage PSD includes regulated mortgage contracts only, therefore excludes unregulated products such as second charge lending, commercial and buy-to-let mortgages.

Impaired credit mortgage

Mortgage lending to a borrower who does not have a standard credit history, ie a recent history of either:

(a) arrears on a mortgage or secured loan. This applies to secured loans where the borrower(s) has arrears on a previous (or current) mortgage or other secured loan within the last two years, where the cumulative amount overdue at any point reached three or more monthly payments; or

(b) arrears on an unsecured loan. This applies to unsecured loans where the borrower(s) has arrears on a previous (or current) mortgage or other secured loan within the last two years where the cumulative amount overdue at any point reached three or more monthly payments; or

(c) Individual Voluntary Arrangement (IVA). This applies where the borrower(s) has been subject to an IVA at any time within the last three years; or

(d) bankruptcy. This applies where the borrower(s) has been subject to a bankruptcy order at any time within the last three years; or

(e) County Court Judgement (CCJ). This applies where the borrower(s) has been subject to a CCJ greater than £500 within the last three years.

Standard variable rate

The rate that is the lender's underlying variable interest rate. This rate is a basic variable rate charged to borrowers with no discounts or other special deals. It is also the rate used by the lender as a reference rate when defining a discounted variable rate product (eg, discounted product ABC is 0.50% below the lender's standard variable or basic rate). This is the rate that mortgage deals will often revert to after a special rate period.

Total gross income

This is the total of the gross annual incomes (before tax or other deductions) of each of the individual borrowers whose incomes were taken into account when the lender made the lending assessment/decision. For these purposes, each borrower's gross income is the sum of that person's main income and any other reckonable income (eg, overtime and/or income from other sources, to the extent that the lender takes such additional income into account in whole or in part).

Tracker

Where the interest rate is guaranteed to move in line with either the Bank of England Base Rate (BBR) or another index such as London InterBank Offered Rate (LIBOR). The rate can track above, below, or at the same level as the index rate.