

Mortgage Market Review Data Pack

Financial Services Authority

Supplement to PS12/16

October 2012



Contents

Foreword	3
Abbreviations and acronyms	4
PART I – Background	
1 Regulatory context of mortgage lending	9
2 Home ownership and mortgage lending	13
3 Economic context of mortgage lending	15
4 Mortgage market diversification	21
5 Lending criteria and ‘mortgage prisoners’	29
PART II – Mortgage performance	
6 Mortgage arrears	37
7 Causes of payment problems	49
PART III – Responsible lending	
8 Income verification	59
9 Income and expenditure	67
10 Mortgage interest rates	75
11 Interest-only mortgages	83
12 Mortgage terms	99
13 Mortgage borrowing and borrowers’ age	103
14 A closer look at self-employed borrowers	111
15 A closer look at first-time buyers	119

16	A closer look at debt consolidation	129
17	A closer look at credit-impaired	135
18	A closer look at right-to-buy mortgages	141
19	A closer look at specialist lenders	149
PART IV – Distribution		
20	Channel of sale and advice	155
PART V – Niche markets		
21	Equity release	167
22	High net worth lending	173
23	Regulated business mortgages	177
Annexes		
Annex 1	Notes on data and methodology	
Annex 2	FSA PSD: Arrears, possessions, concessions and arrangements data request	

Foreword

This is the final data pack published as a supplement to the Mortgage Market Review (MMR) Policy Statement (PS12/16).

It contains statistical evidence which has been used to help inform our policy analysis throughout the MMR. It is based on the data pack for CP11/31, updated with 2011–2012 data, where available.

The Mortgage Market Review Policy Statement can be found here:

www.fsa.gov.uk/Pages/Library/Policy/Policy/2012/12-16.shtml

Copies of this document are available to download from our website: www.fsa.gov.uk.

Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

Abbreviations used in this paper

BoE	Bank of England
BTL	Buy-to-let
CBA	Canadian Bankers Association
CCJ	County Court Judgement
CDS	Credit Default Swap
CML	Council of Mortgage Lenders
DCLG	Department for Communities and Local Government
DWP	Department for Work and Pensions
EFS	Expenditure and Food Survey
EMF	The European Mortgage Federation
ER	Equity Release (plan)
FPC	Financial Policy Committee
FSS	Financial Strategy Segments
FTB	First-time buyer
HMRC	Her Majesty's Revenue and Customs
HNW	High Net Worth
HPP	Home Purchase Plan
HRP	Home Reversion Plan
IVA	Individual Voluntary Agreement
LCF	Living Cost and Food Survey
LHS	Left-hand side (axis)
LTI	Loan-to-income (multiple)

LTV	Loan-to-value (ratio)
MIRAS	Mortgage Interest Relief at Source
MLAR	Mortgage Lending and Administration Return
NFI	Non-financial Institutions
NI	National Insurance (contributions)
NMG	NMG Financial Services Consulting
NSA	Not seasonally adjusted (data)
OECD	Organisation for Economic Cooperation and Development
ONS	Office for National Statistics
PSD	Product Sales Data
PTI	Price-to-income (multiple)
RBA	Reserve Bank of Australia
RHS	Right-hand side (axis)
RMS	Regulated Mortgage Survey
RTB	Right-to-buy
SBS	Survey of Building Society Mortgages
SHIP	Safe Home Income Plans
SMI	Support for Mortgage Interest
SML	Survey of Mortgage Lenders
SRB	Sale and Rent Back
SVR	Standard Variable Rate

PART I

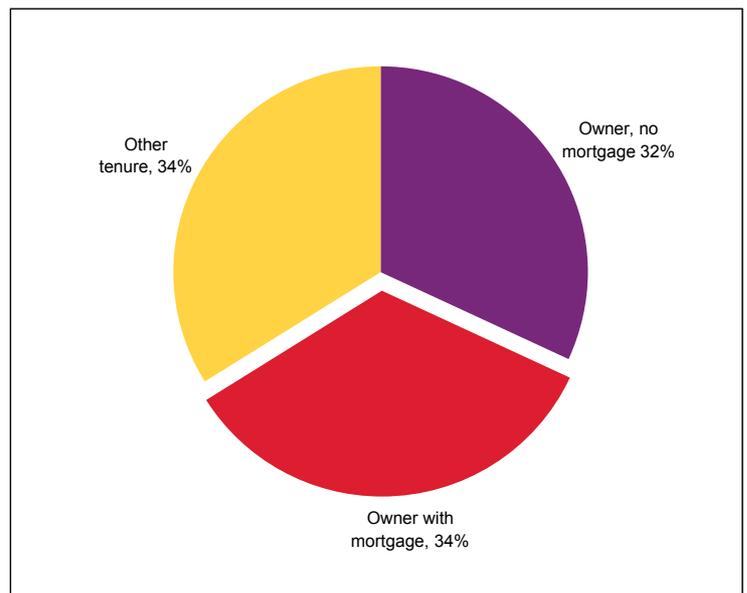
Background

1

Regulatory context of mortgage lending

- According to the ONS, as of 2011, there were approximately 26.3m households in the UK.
- Of these, 66% are home owners, made up of 32% who own their home outright and 34% who have a first-charge mortgage.
- The remaining 34% are private or social tenants.
- This means that today around 8m own their homes outright, 9m own their homes with a mortgage and 9m rent.

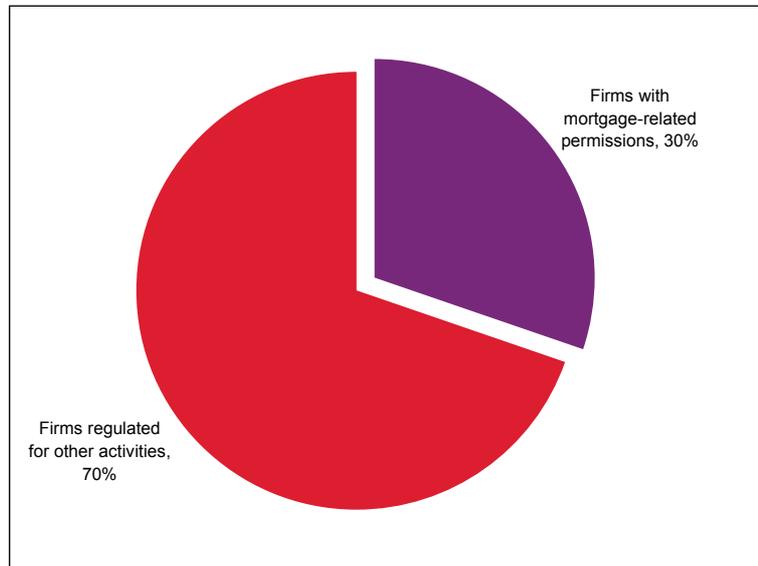
Exhibit 1.1: Structure of house tenure, 2011



Source: DCLG

- Nearly a third of firms we authorise are regulated for at least one home finance activity.
- In September 2012, there were around 6,000 firms with mortgage-related permissions.

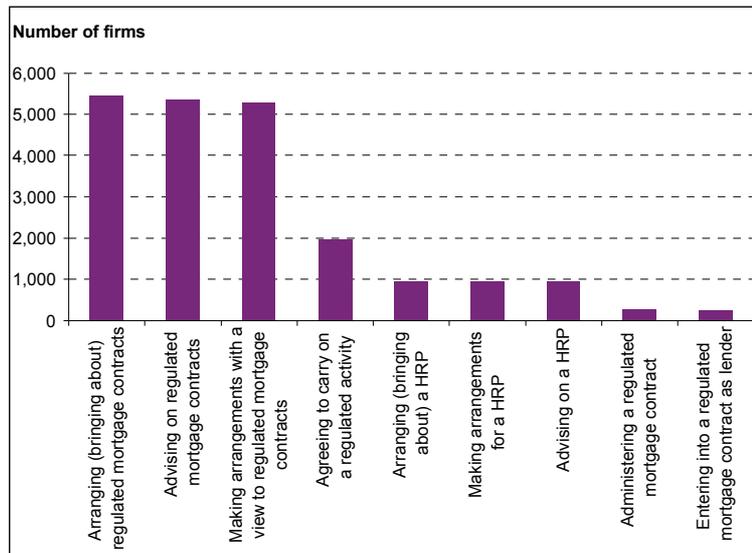
Exhibit 1.2: Firms regulated by the FSA, September 2012



Source: FSA

- Of these, most are regulated for advising and arranging regulated mortgage contracts.
- Firms regulated for home reversions, sale and rent back and Home Purchase Plan (HPP) activities make up the smallest group.
- More information on the types of regulated home finance activities can be found in the FSA Handbook¹.

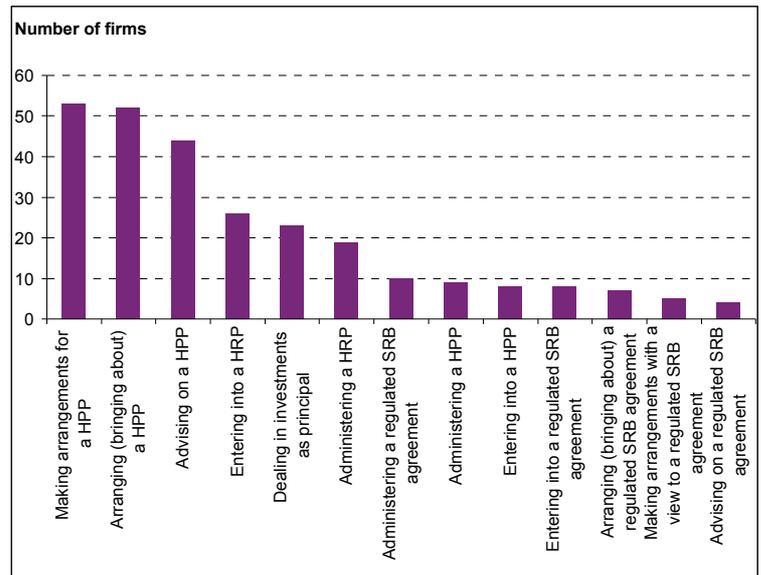
Exhibit 1.3: Regulated home finance firms and activities, September 2012 (part 1)



Source: FSA

¹ See FSA Handbook, Guidance on regulated activities connected with mortgages (PERG 4) available at <https://fsahandbook.info/FSA/html/handbook/PERG/4>

Exhibit 1.4: Regulated home finance firms and activities, September 2012 (part 2)



Note: On Exhibits 1.3 and 1.4 we show numbers of firms on two different scales for clarity, as the numbers of firms shown in Exhibit 1.4 are comparatively small.

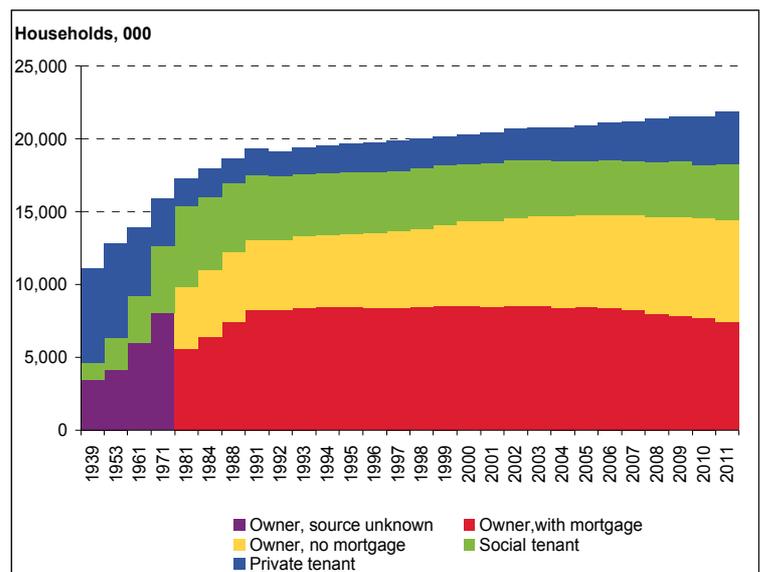
Source: FSA

2

Home ownership and mortgage lending

- Over the last century, property tenure in the UK has undergone major structural change.
- The number of households has doubled from the 1939 levels due to population growth and the social and lifestyle changes discussed below.
- Property ownership increased dramatically – 66% of UK households now own their home, compared to only a third of households in the early 1950s.
- Home ownership was encouraged by government initiatives such as, Mortgage Interest Relief at Source (MIRAS) and right-to-buy (RTB).²

Exhibit 2.1: Evolution of tenure in the UK, number of households

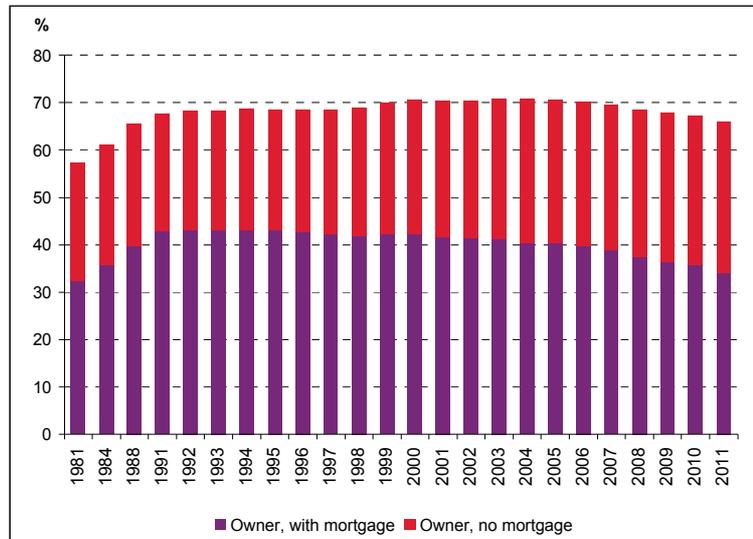


Source: DCLG

² See Chapter 18 of this data pack for more information on RTB mortgages

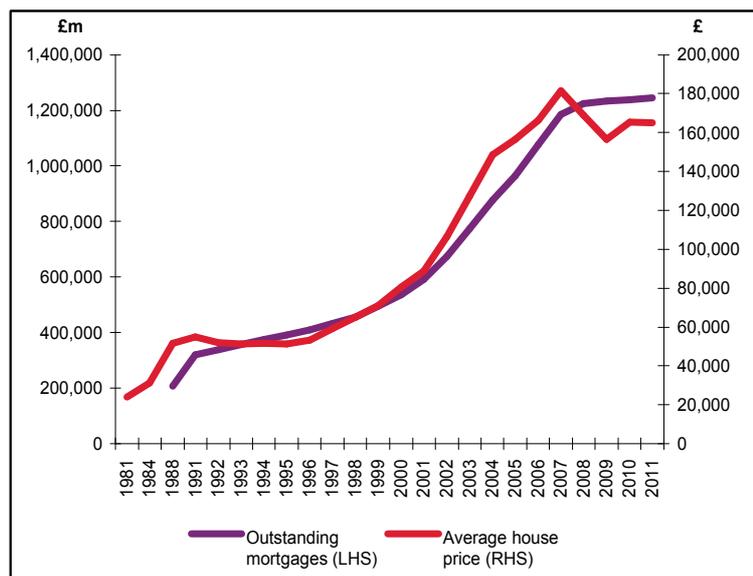
- The current level of home ownership was reached in the early 1990s and has since remained relatively flat. Proportionally, ownership with a mortgage has, in fact, been declining and outright ownership has been increasing since the mid-1990s.
- There are several reasons for this trend, both demographic and economic. For example, an ageing population means that there are more older home owners who have paid off their mortgages or have been able to buy their next property outright, some cashing in on the increased values of their previous homes.
- At the same time, rising house prices have meant that some younger households have been temporarily or permanently priced out of the market. Both trends have led to a reduction in the proportion of households that required a mortgage.
- The enormous increase in mortgage lending and household debt over the past ten years was mainly driven by house price rises – it did not increase home ownership.

Exhibit 2.2: Home owners, by type



Source: DCLG

Exhibit 2.3: Outstanding mortgages and average house prices



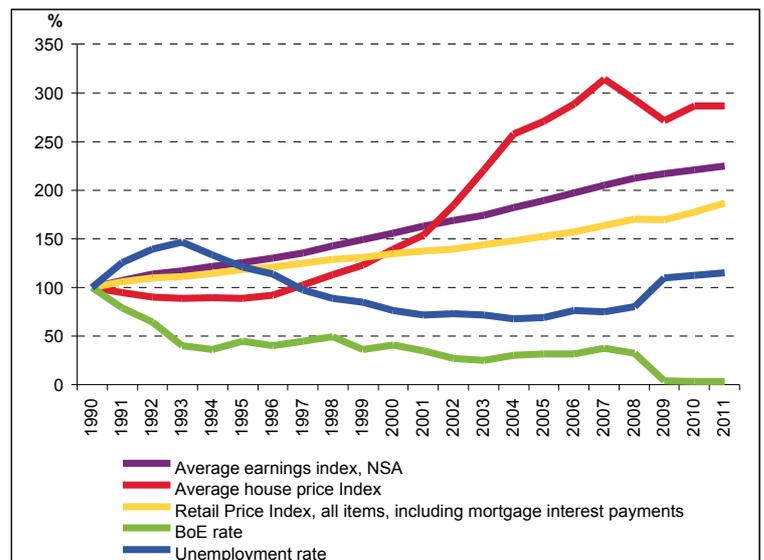
Source: BoE, Nationwide

3

Economic context of mortgage lending

- Economic conditions provided a favourable background for mortgage market growth from the mid-1990s.
- Falling interest rates, lower unemployment and increased average earnings meant that market confidence was high.
- A positive economic outlook enhanced consumer optimism, led consumers to take on increasing amounts of debt, and encouraged greater lending volumes.

Exhibit 3.1: Key economic indicators

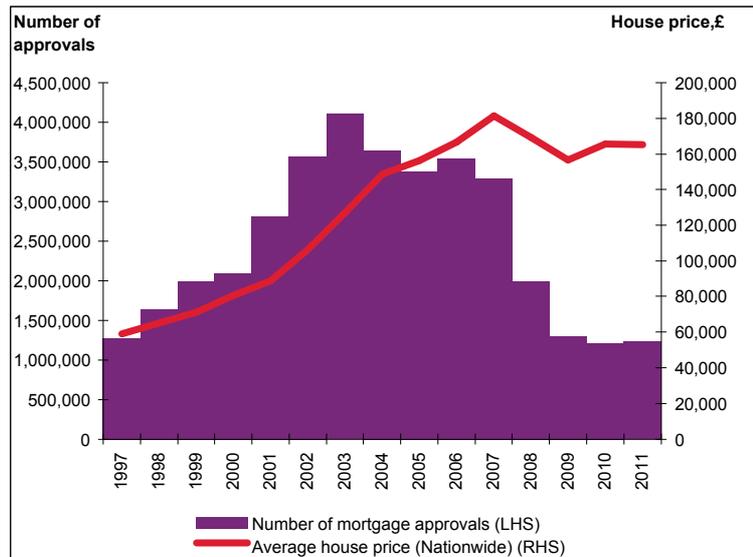


Note: Baseline 1990=100%

Source: Nationwide, ONS, BoE, FSA calculation

- With rising property prices from the mid-1990s, the demand and supply of credit increased, with lenders receiving and approving a consistently high number of mortgage applications.
- This trend continued until the market downturn in 2008.

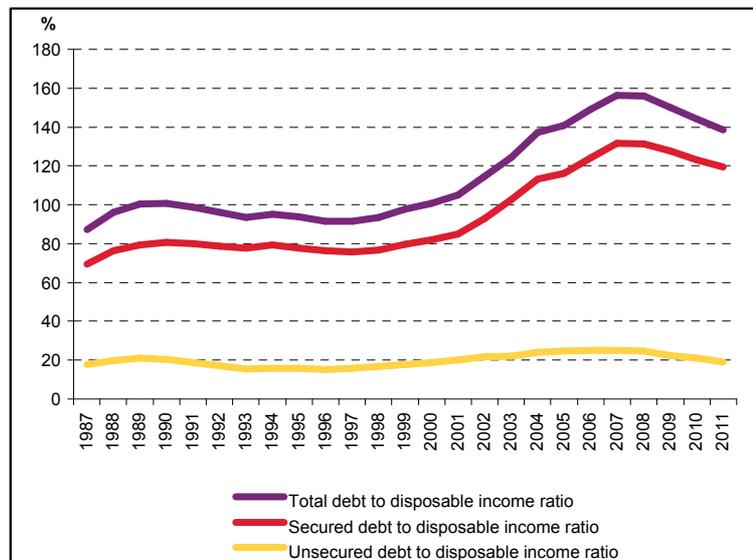
Exhibit 3.2: Mortgage approvals and house prices



Source: BoE, Nationwide

- Borrowers extended their secured debt way beyond previous levels as demand for mortgages remained high, interest rates stayed relatively low and house prices grew.
- In 2011, secured debt was 119% of households' annual disposable income, having risen from 80% in 2000.
- Unsecured debt commitments relative to household disposable income were stable over a long period of time, although there has also been a slight upward trend from the late 1990s.

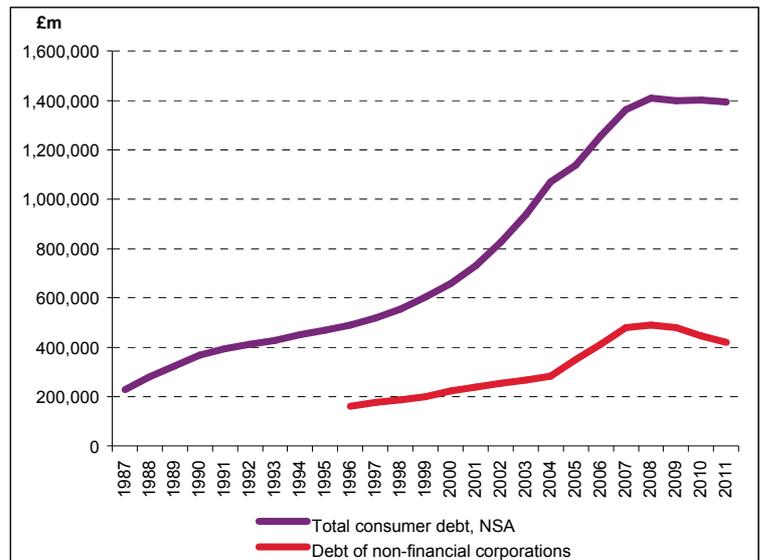
Exhibit 3.3: Secured and unsecured debt to disposable income ratios



Source: ONS

- Residential mortgage debt in the UK now amounts to around £1.25trn, accounting for approximately 70% of all credit extended by lenders to households and non-financial businesses in the UK.

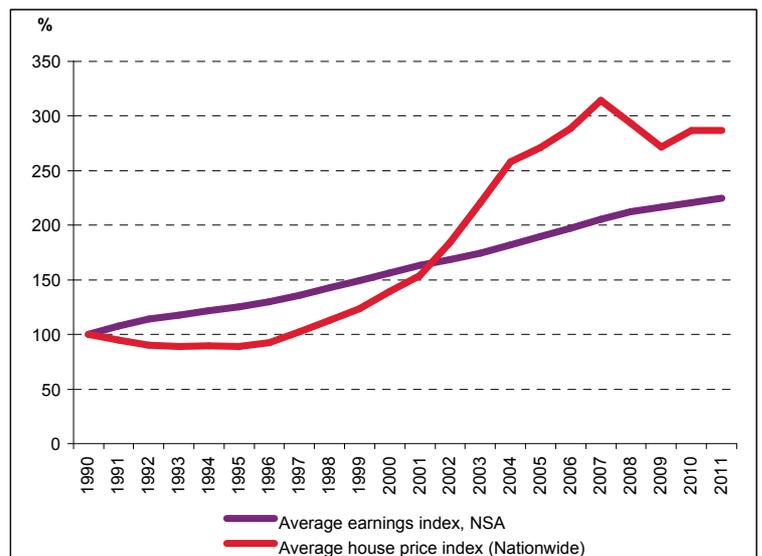
Exhibit 3.4: Secured and unsecured debt held by households and non-financial businesses in the UK



Source: ONS

- There were winners and losers as a result of this growth in the market.
- As house prices were rising at a much faster pace than average income, would-be buyers increasingly had to stretch themselves in order to buy a house.

Exhibit 3.5: Average house prices and average earnings

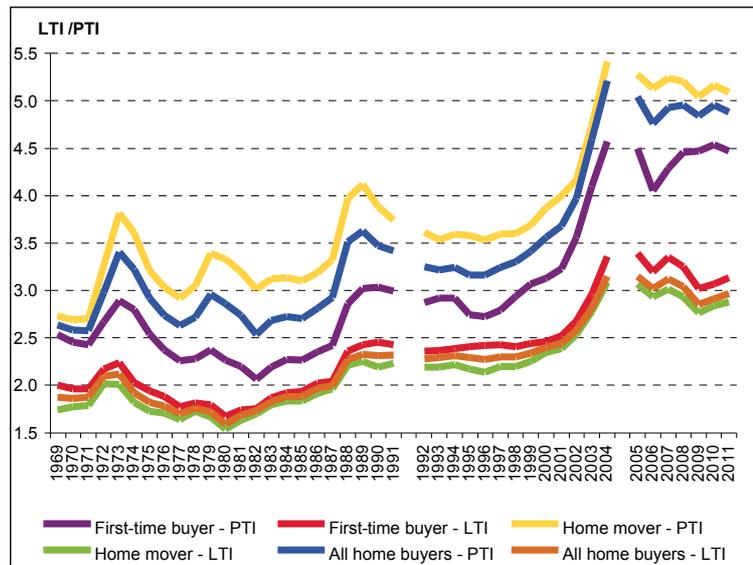


Note: Baseline 1990=100%

Source: ONS, Nationwide

- In 2011, an average house was worth approximately five times the income of the average house buyer. This compares to 3.7 times income ten years before. As a result, households had to borrow more and income multiples increased.
- At the same time, those already on the property ladder benefited from increased house prices.

Exhibit 3.6: Average Loan-to-Income (LTI) and Price-to-Income (PTI) multiples, by borrower type

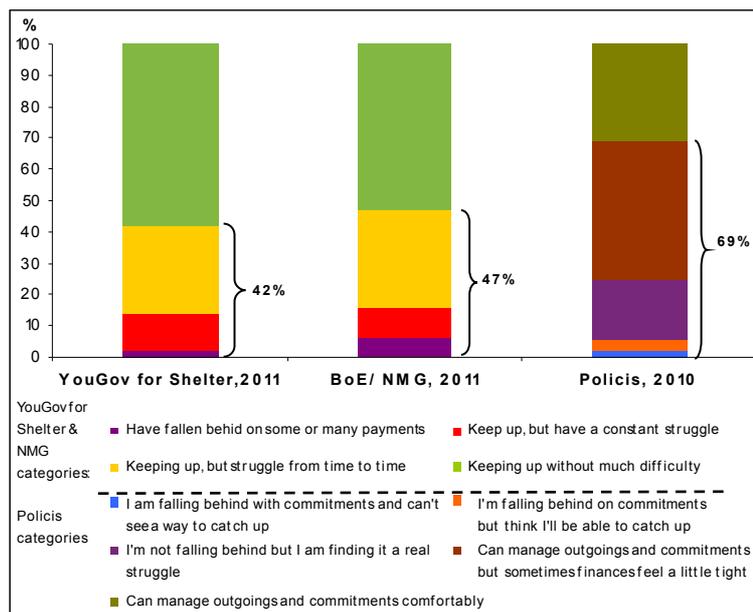


Note: Ratios up to and including 1987 have been calculated using the aggregated simple average prices, advances and incomes. Ratios from 1988 have been calculated on a case-by-case basis and then averaged. Spaces indicate breaks in series as the data is from three different surveys (SBS, SML, RMS)

Source: DCLG, ONS

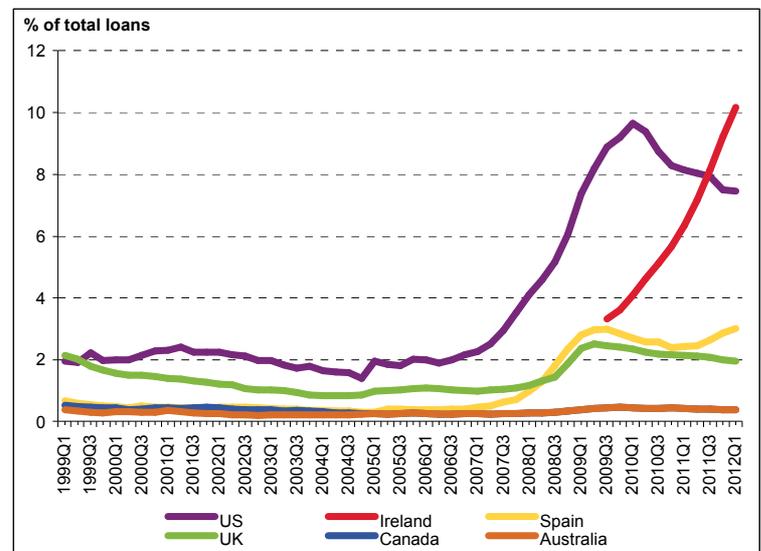
- Despite low interest rates, many mortgage borrowers are financially overstretched and are finding it increasingly difficult to meet their ongoing financial commitments.
- In 2010, 69% of mortgage borrowers according to a Policis survey and in 2011, 47% according to a Bank of England (BoE) & NMG survey, struggled to pay their bills and commitments at least from time to time. This includes 22% and 16% respectively that struggled constantly or were falling behind with their payments.
- The results from the 2011 YouGov survey for Shelter suggest that 42% of borrowers struggle to make mortgage payments at least from time to time, with 14% struggling constantly or falling behind.

Exhibit 3.7: Extent to which mortgage borrowers are struggling to keep up with their payments



Source: BoE/NMG, Policis, YouGov online survey for Shelter (GB representative, 4,014 respondents, December 2011), FSA analysis

- Between 2002 and 2007, many OECD economies, including the UK, experienced housing bubbles as house prices and indebtedness rose rapidly.
- Across the US, Ireland, Spain, UK, Canada and Australia, house prices and debt-to-income levels increased at similar rates. However, the bursting of these housing bubbles has been followed by varying levels of default and pain for both lenders and borrowers.
- Macroeconomic conditions alone are unable to fully explain these differences. Deterioration in lending standards, characterised by the growth in risky lending practices, such as self-certification of income, reliance on house price increases and lending to risky borrower types, have been the main drivers of the high default levels in the US, Ireland, Spain and UK³ so far.

Exhibit 3.8: Mortgage arrears of 90+ days, by country

Source: US Federal Reserve, Irish Central Bank, Fitch, CML, RBA, CBA

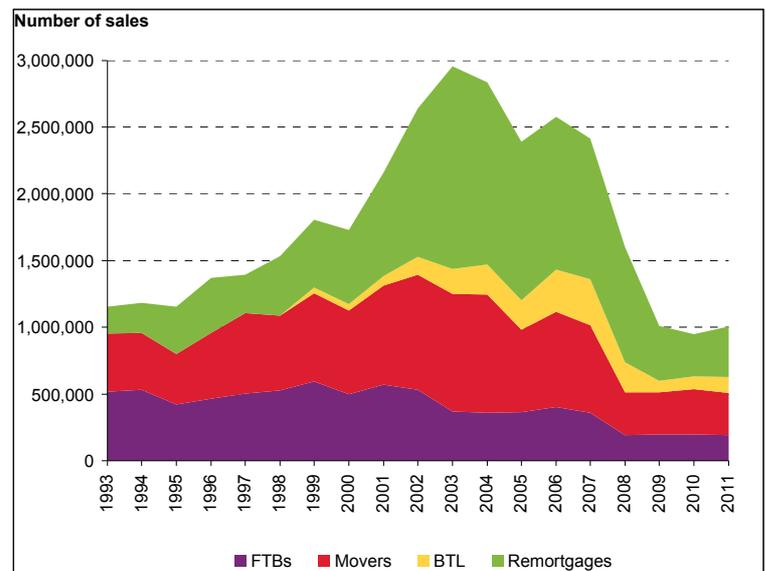
³ More information on arrears and repossessions in the UK is available in Chapter 6 of this data pack.

4

Mortgage market diversification

- Although traditionally mortgages were designed to help people buy houses, not all mortgages are used for this purpose.
- At the peak of the market, nearly half of all mortgages went to remortgagors – looking for better deals or taking equity out of their properties which were rapidly increasing in price.

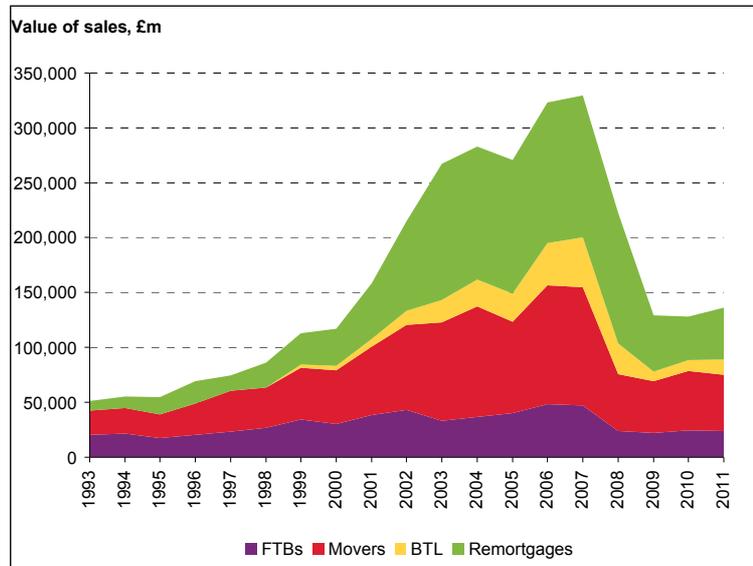
Exhibit 4.1: Mortgage lending by purpose, number of sales



Source: CML

- Over the past 20 years up to 2007, lending for house purchase has not changed significantly in terms of the numbers of households taking out mortgages (see Exhibit 4.1). However, it did increase considerably in terms of lending values as houses have become more expensive.

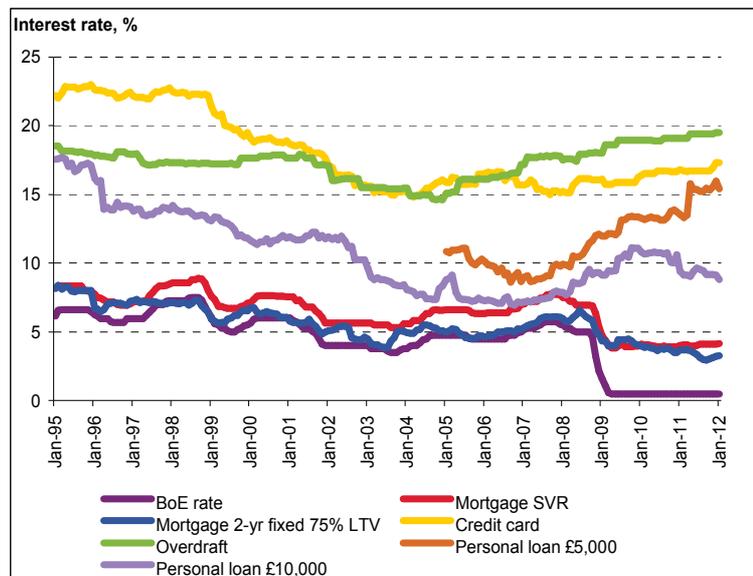
Exhibit 4.2: Mortgage lending by purpose, value of sales



Source: CML

- Historically, mortgage credit has been the cheapest form of credit available to households.

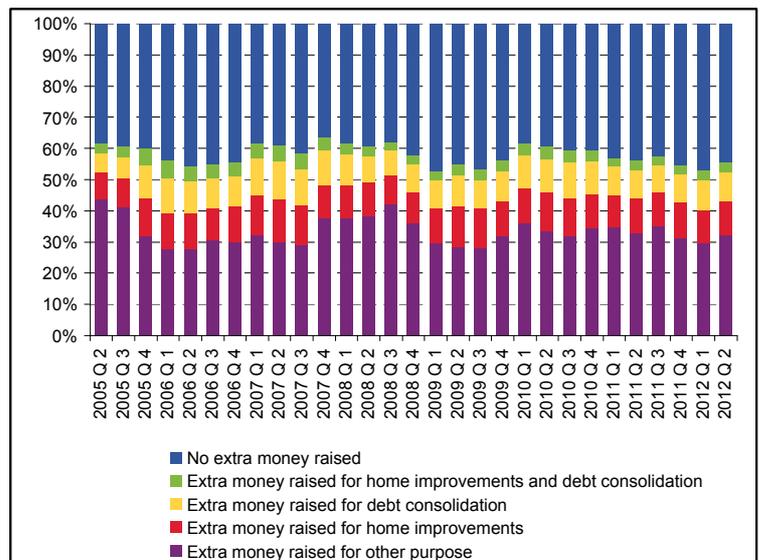
Exhibit 4.3: Price of credit, by type



Source: BoE

- Therefore, many households used mortgages as a cheaper alternative to consumer credit products.
- Around 60% of borrowers take out extra money when they remortgage.
- Further advances are another popular choice that allow mortgage borrowers to increase their mortgage at a later stage for needs unrelated to house purchase.
- In 2007-2012, the average further advance was around £25,000 and around 20% of all new mortgage accounts by number (5% by value) were further advances.

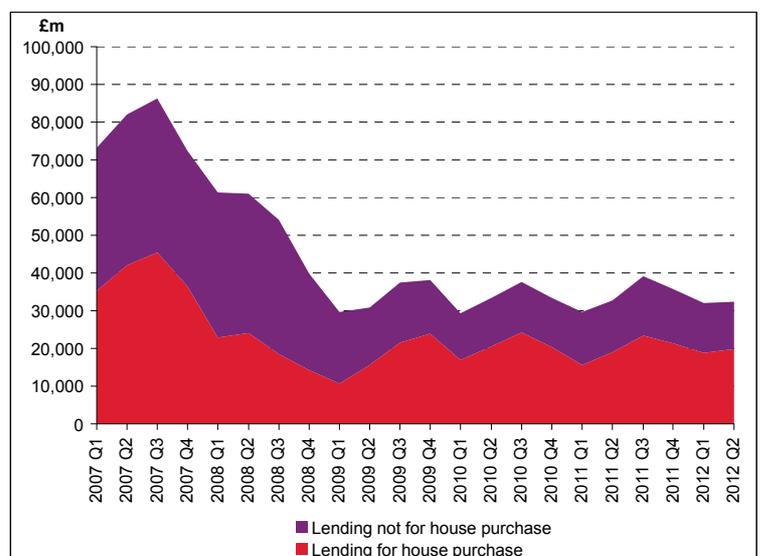
Exhibit 4.4: Structure of remortgage sales, by purpose



Source: FSA PSD

- In the last five years, about half of all mortgage lending by value was not used to buy houses. In 2007, this amounted to nearly £155bn.

Exhibit 4.5: Mortgage lending, by purpose

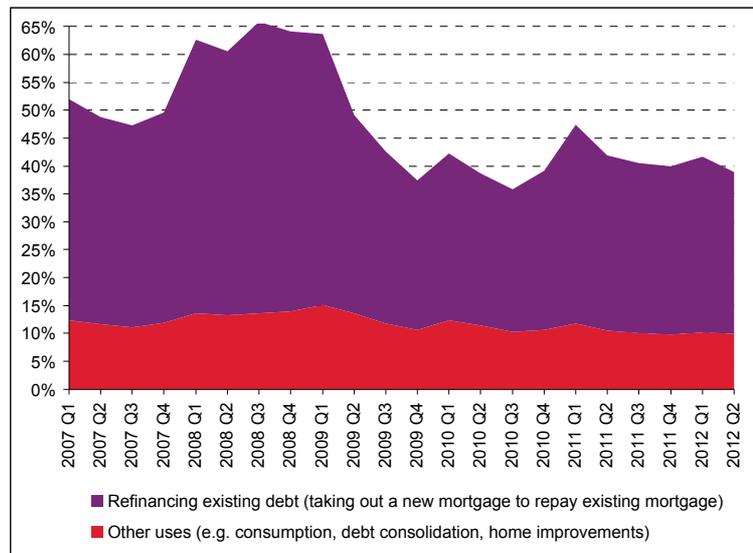


Note: Regulated mortgages only

Source: FSA MLAR, FSA PSD, FSA estimates

- Most of this lending was simple like-for-like remortgaging for a better rate. This is because a sizeable difference between initial mortgage rates and SVRs before the market downturn encouraged borrowers to seek better rates after their initial deals had ended.
- Around 12% of mortgage lending was spent on consumption, e.g. to support lifestyles, to pay for home improvements or to consolidate debts.
- Since 2009, the proportion of lending for like-for-like remortgaging has reduced considerably as low SVRs removed the incentive for some borrowers to seek a better rate. Mortgage lending used for consumption did not reduce in proportional terms.
- As lending margins became increasingly tight due to the high levels of competition, frequent remortgaging created a steady stream of income both for lenders (through upfront fees) and for brokers (through commission).
- In the run-up to the crisis, low headline interest rates on mortgages became a strong marketing feature as firms competed for market share. This resulted in a situation where turnover from interest was sacrificed for an increase in non-interest income.

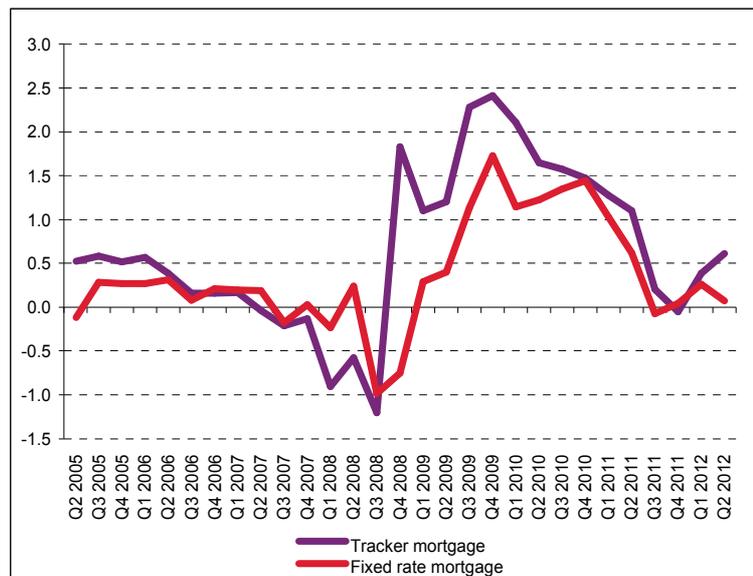
Exhibit 4.6: Proportion of mortgage lending for purposes other than house purchases



Note: Regulated mortgages only

Source: FSA MLAR, FSA PSD, FSA estimates

Exhibit 4.7: Indicative interest rate mark-up on residential mortgages



Note: This Exhibit shows indicative interest rate mark-up, expressed in percentage points. For illustration purposes only, we define mark-up as follows:

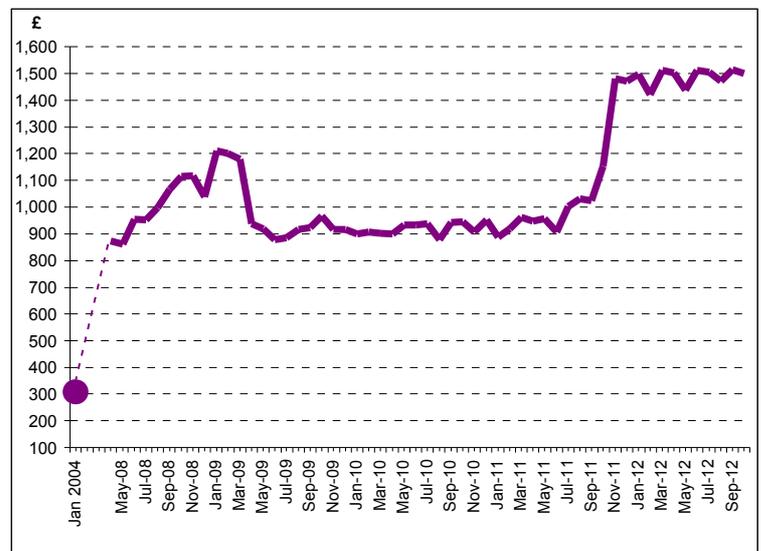
Tracker mortgage mark-up - this is the estimated margin for extending sterling-denominated 75% LTV tracker mortgages. It is the difference between the quoted retail rate and the marginal cost, which is the sum of three-month Libor plus an average of the five-year CDS premia of the major UK lenders (Banco Santander, Barclays, HSBC, Lloyds Banking Group, Nationwide and RBS).

Fixed rate mortgage mark-up - this is the estimated margin for extending fixed rate sterling-denominated mortgages. It is the difference between the quoted retail rate and the marginal cost, which is the sum of five-year swap rate plus an average of the five-year CDS premia of the major UK lenders (Banco Santander, Barclays, HSBC, Lloyds Banking Group, Nationwide and RBS).

Source: BoE, Bloomberg, Datastream, FSA estimate

- Towards the end of 2007, product fees became an important feature of the pricing and design of mortgage products.
- Historically, products were evenly priced throughout the market, with average arrangement fees around £309 in 2004.
- By October 2012, the average product fee had increased to £1,501.

Exhibit 4.8: Average mortgage arrangement fee

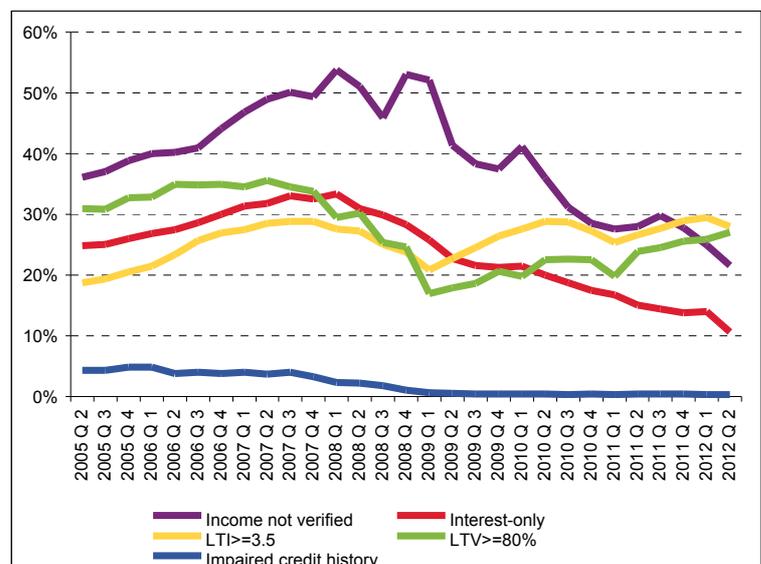


Note: (1) Average mortgage arrangement fee for January 2004 is based on 915 products; (2) Data excludes fee-free products. We estimate that in 2008-2011, around 15% of mortgage products in the mainstream market were fee-free.

Source: Defaqto (2004), Moneyfacts (2008-2012)

- In a chase for higher returns, lenders took increasingly higher risks. For example, in 2007, over 50% of mortgages were sold with no verification of income and over 30% had LTVs in excess of 80%.

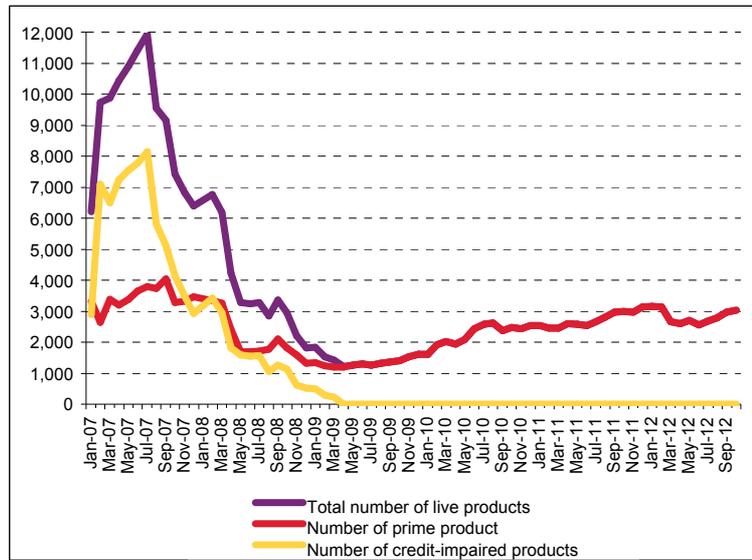
Exhibit 4.9: Proportion of higher-risk sales in total mortgage sales



Source: FSA PSD

- The number of mortgage products on offer increased dramatically, particularly in the subprime sector where margins were higher.

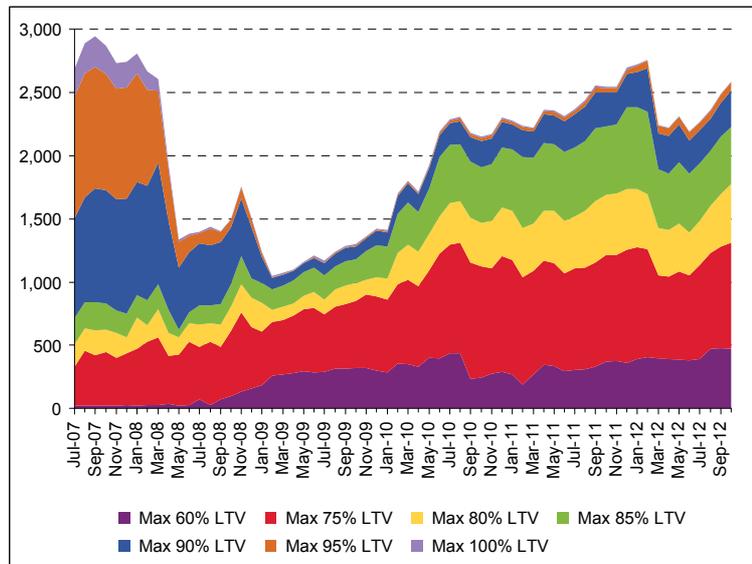
Exhibit 4.10: Number of residential mortgage products



Source: Moneyfacts

- Many high LTV products were on offer. For example, in 2007, 44% of products permitted LTVs of 95% or higher. This reduced to 1.2% in 2010.
- Recently we have seen a return of some higher LTV mortgages, particularly in the LTV bands up to 80% and 85%.
- However, the availability of mortgage products at very high LTVs in excess of 85% remains limited. This may change in the future in response to the new build indemnity scheme⁴ that is designed to help provide up to 95% LTV mortgages for newly built properties in England.

Exhibit 4.11: Number of prime residential mortgage products, by LTV

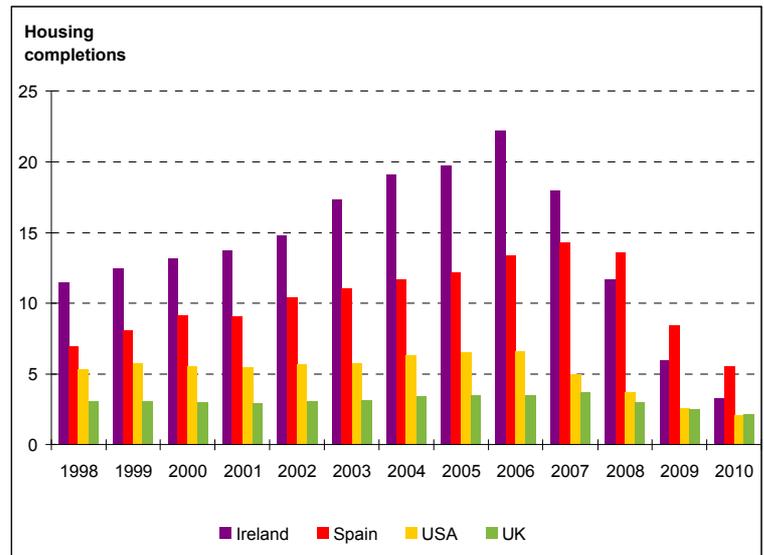


Note: This Exhibit does not show LTV bands other than noted above.

Source: Moneyfacts

⁴ Under the proposals in the Housing Strategy announced by the government in November 2011, homebuyers will be able to secure loans on newly built homes with only 5% deposit. For more information on the Housing Strategy see www.communities.gov.uk/news/corporate/2033724

- Readily available cheap credit meant that more people were competing for the same number of available properties.
- As a result, house prices tripled between 1990 and 2007 and far outstripped average earnings (see Exhibit 3.5).
- Unlike the other countries referred to in Exhibit 4.12, the UK has not experienced a construction boom.
- Constraints in supply coupled with an increase in the number of households may also have contributed to the house price rises.

Exhibit 4.12: Housing completions per 1,000 inhabitants

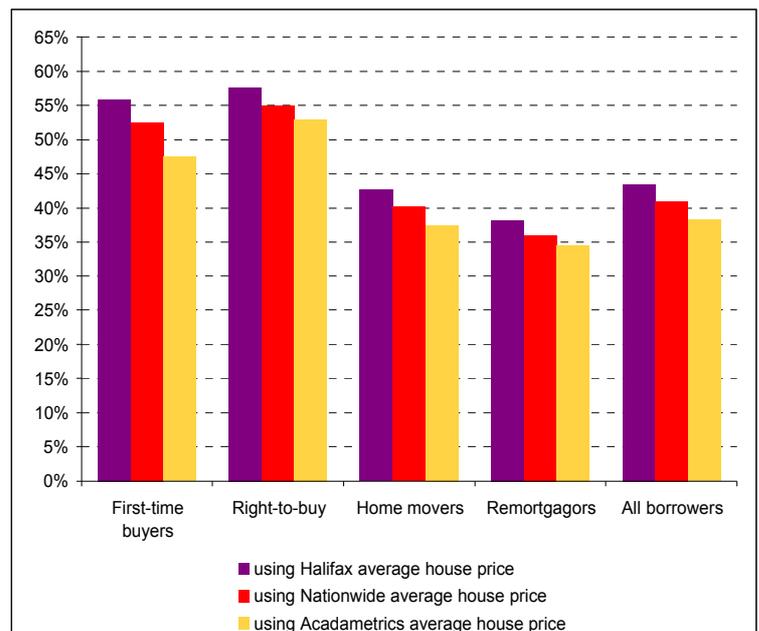
Source: EMF

5

Lending criteria and ‘mortgage prisoners’

- As a result of lenders’ post-crisis voluntary tightening of lending criteria, by March 2012, we estimate that up to 45% of those borrowers who had taken out a mortgage since 2005 could be ‘mortgage prisoners’⁵.
- This figure may be even higher for former first-time buyers (FTBs) - we estimate that around 55% could be ‘mortgage prisoners’.
- This means that these borrowers may not be able to remortgage for a better deal or move house.

Exhibit 5.1: ‘Mortgage prisoners’, by borrower type



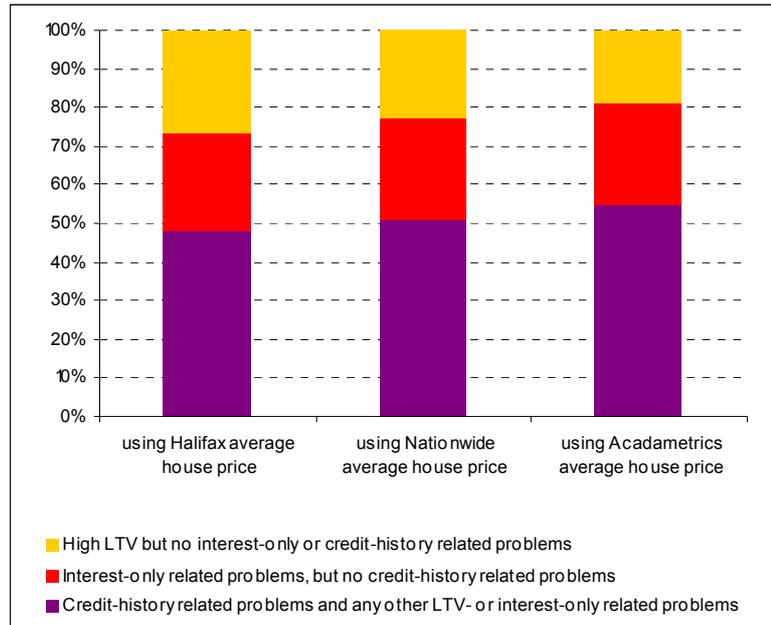
Note: Borrowers who obtained mortgages in April 2005 – December 2011 only

Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

⁵ See Annex 1 for the summary of the methodology that we followed to work out the estimates presented in this Chapter.

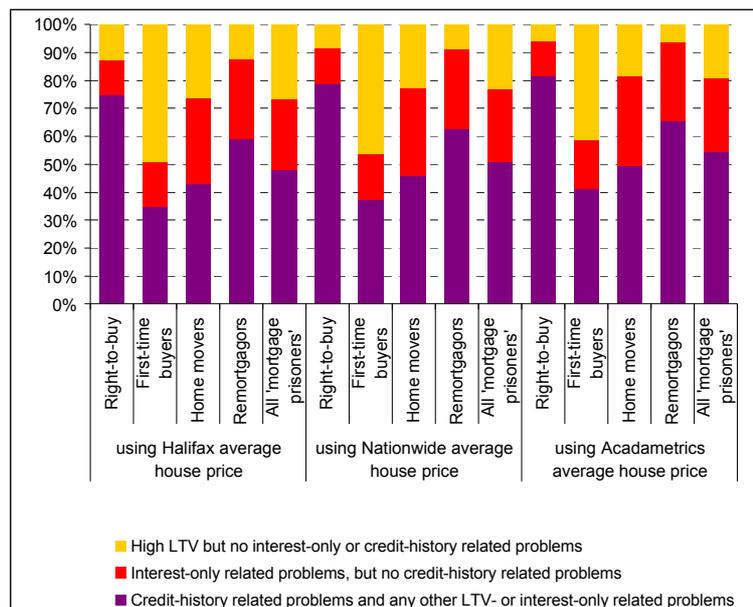
- Currently, half of ‘mortgage prisoners’ are in this situation because they could have credit history problems. The remaining half are affected by the limited availability of interest-only and high LTV products.
- However, this depends on the type of borrower. For example, nearly half of former first-time buyers could be ‘mortgage prisoners’ because they would require higher-LTV mortgages.

Exhibit 5.2: 'Mortgage prisoners' - reasons



Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

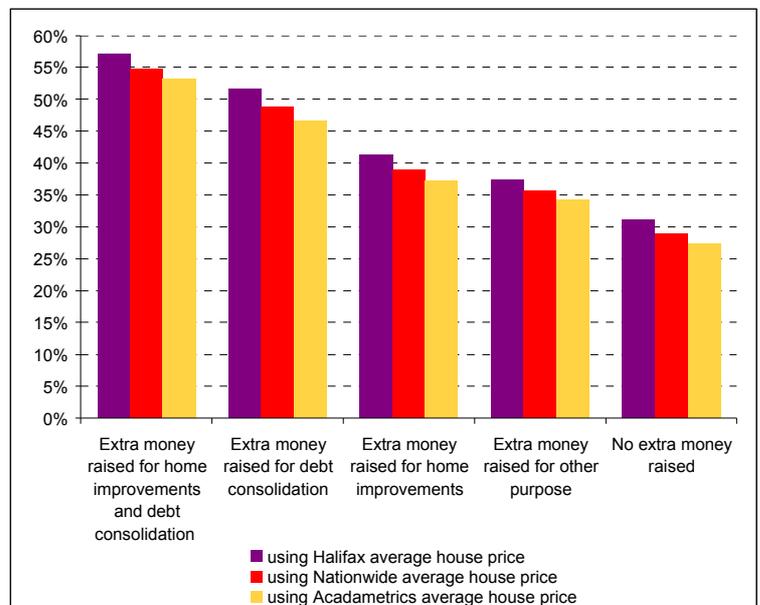
Exhibit 5.3: 'Mortgage prisoners', by borrower type - reasons



Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

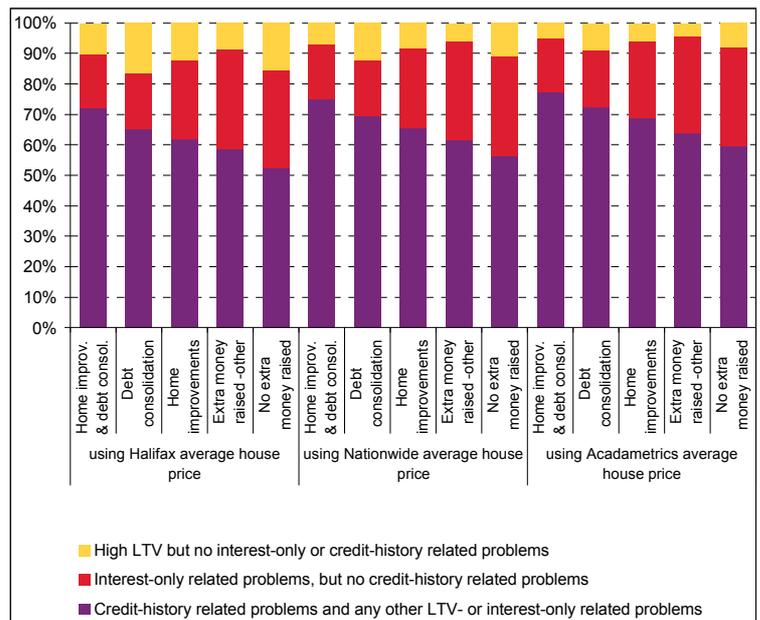
- For remortgagors, again, the reasons for being ‘mortgage prisoners’ depend on the type of remortgage.
- Generally, a much larger proportion of borrowers who withdrew equity in the past are now ‘mortgage prisoners’, with a very significant proportion of borrowers in this situation not just because of the limited availability of interest-only or high LTV mortgages, but also because of a past or recent history of payment problems.

Exhibit 5.4: ‘Mortgage prisoners’ – remortgagors



Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

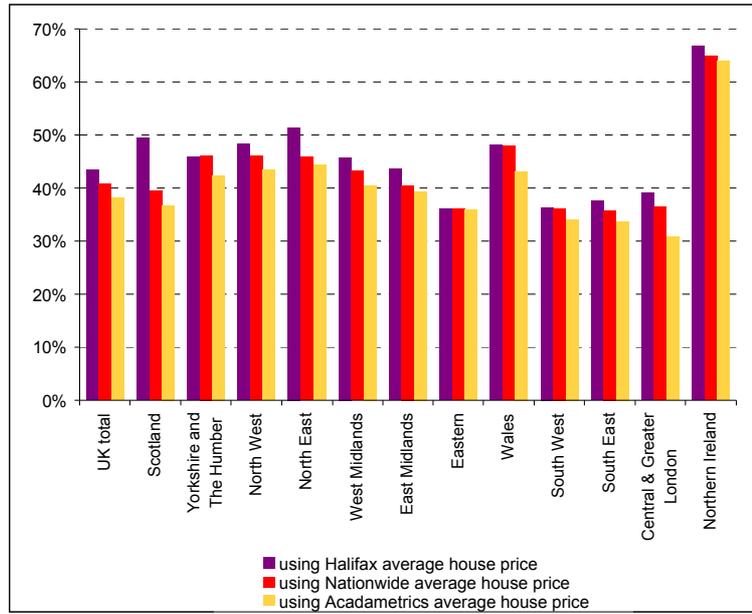
Exhibit 5.5: ‘Mortgage prisoners’, remortgagors by purpose - reasons



Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

- More people in the north than in the south may find it difficult to remortgage. This may reflect the past structure of borrowing in these regions, with more borrowers taking out high LTV or interest-only mortgages.

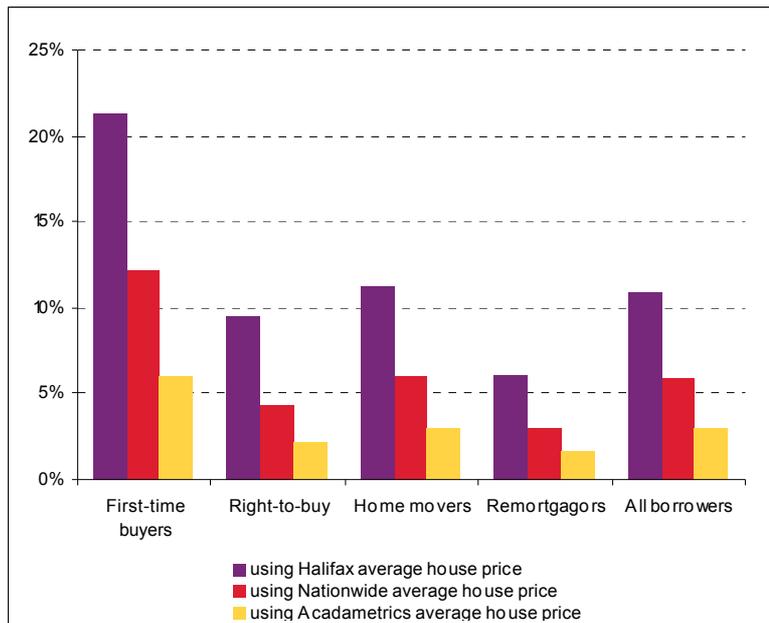
Exhibit 5.6: ‘Mortgage prisoners’, by region



Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

- We estimate that over 10% of those who borrowed in 2005-2011 could be in negative equity, including over 20% of former FTBs.
- Borrowers who took out high LTV interest-only mortgages at the peak of the market are particularly affected.

Exhibit 5.7: Negative equity, by borrower type, Q1 2012

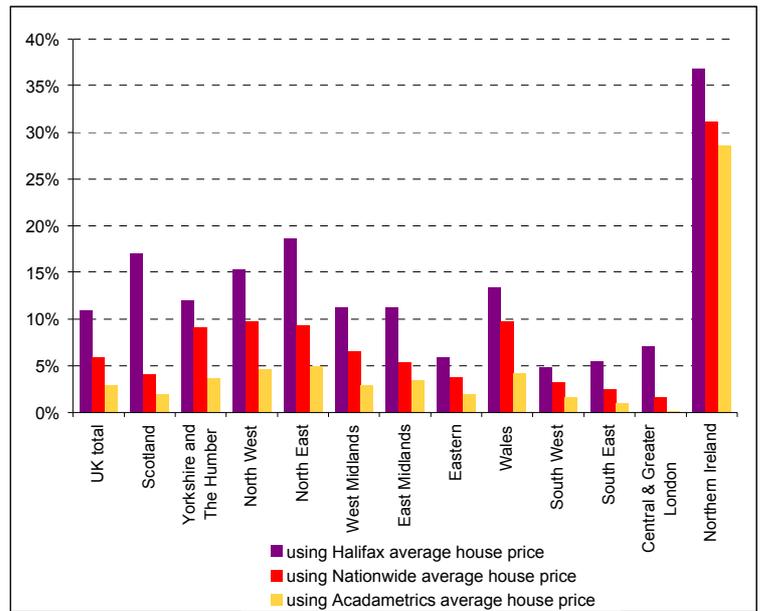


Note: Borrowers with current (indexed) LTV >100%

Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

- Regionally, more households in the north than in the south could be in negative equity.

Exhibit 5.8: Negative equity, by region, Q1 2012



Note: Borrowers with current (indexed) LTV >100%

Source: PSD Performance data 2012, Acadametrics, Halifax, Nationwide, FSA estimates

PART II

Mortgage performance

6

Mortgage arrears

There are various sources of data on mortgage arrears and payment difficulties that suggest somewhat different views on the numbers of households that could be falling behind with their mortgage payments.

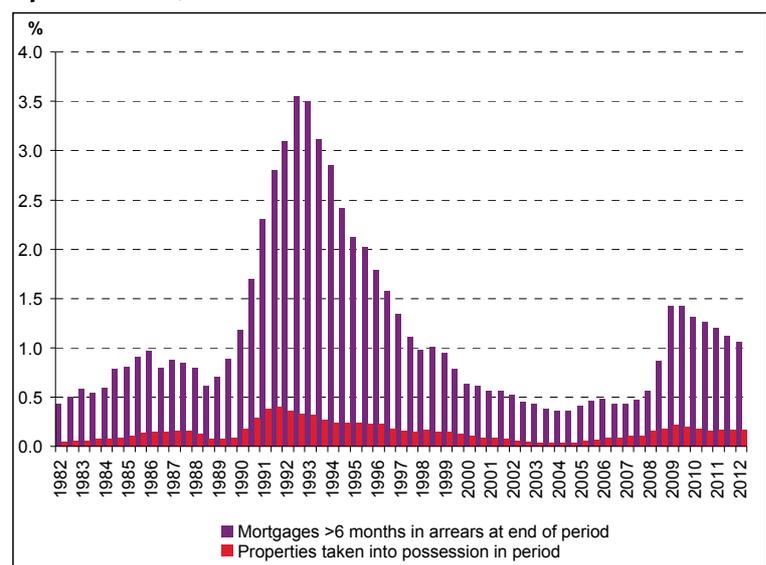
In this Chapter and throughout this data pack, we use different data sources to illustrate the extent of payment problems in the mortgage market. Some of this data, published by the FSA and by the CML, is widely regarded as official statistics on mortgage arrears and repossessions and could be well known to readers. Other data comes from consumer surveys and provides more insight into the financial circumstances of households not captured by official statistics.

Additionally, we use transactional data on the performance of regulated mortgages sold in April 2005-December 2011 that we have collected from lenders, with help from the CML. This data is extremely detailed and allows us to look at mortgage performance across a range of various borrower and product characteristics.

More information on our data and methodology is set out in Annex 1 to this data pack.

- Mortgage lending is not risk free for lenders and borrowers. Some consumers taking out mortgages may not be able to keep up with repayments and some may lose their homes as a result.
- The reasons for arrears vary. At an aggregate level, the level of arrears could be explained by the risk appetite of lenders and by the state of the economy. At an individual level, the likelihood of arrears could depend, for example, on a borrower's level of income, savings and borrowing, lifestyle, family situation, budgeting skills and stability of employment.
- The CML has almost 30 years worth of data on severe arrears of more than six months and repossessions.

Exhibit 6.1: Severe arrears of over 6 months and repossessions, 1982–H1 2012



Note: (1) This Exhibit shows the percentage of total number of first charge mortgages (owner occupier and buy-to-let)

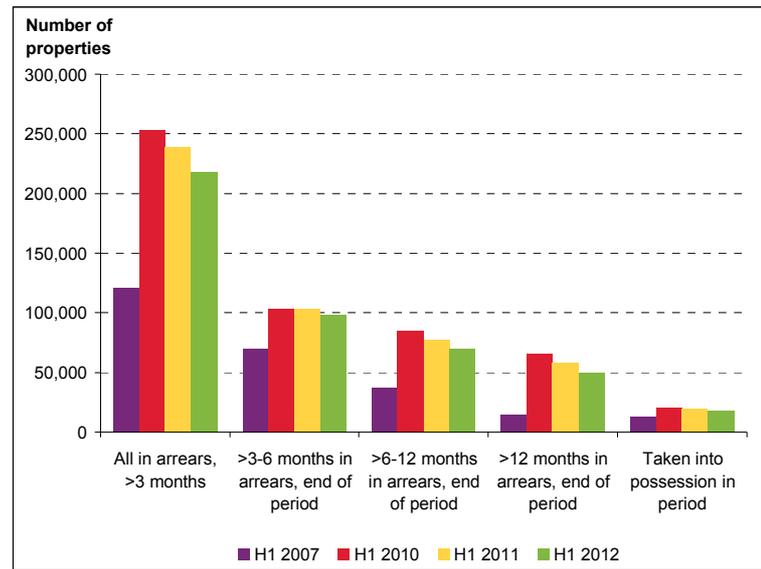
- This indicates that residential mortgage arrears increased between 2008 and early 2012 - but appear to have peaked at well below 1990 to 1992 levels.
- Similarly, repossessions are below the levels seen in the 1990s.
- The lower arrears and repossessions that we have seen during this downturn are primarily explained by two factors.
- First, mortgage interest rates (which increased dramatically between 1988 and 1990) have fallen in this downturn. This has resulted in improved mortgage affordability.
- Second, the overall unemployment rate is not as high as in the early 1990s. Moreover, the most significant increases in unemployment have occurred in the 16-24 year-old age group, which is minimally exposed to mortgage debt (see Exhibit 7.3).
- Within the overall favourable picture today, however, it is important to note three caveats:
- first, lenders' forbearance may be disguising the scale of the problems;
- second, experience has varied considerably by region and customer segment (discussed further on in this data pack); and
- third, the picture may change quickly, particularly when interest rates rise.
- Despite historically low interest rates and lower unemployment, there was a significant increase in financial distress in 2010-2012 compared with 2007, with a higher proportion of longer-term arrears.

Note: (2) Unemployment, interest rates and forbearance in 1990s and 2009.

	1990s	2009
Unemployment	3m (1993)	2.4m
Average interest rate	15.2% (1990)	3.81% (Q4 2009 outstanding mortgages) 3.97% (Q4 2009 gross advances)
Forbearance	Unknown	Extent of forbearance is significant given pressure from government, courts and FSA to help borrowers in difficulty

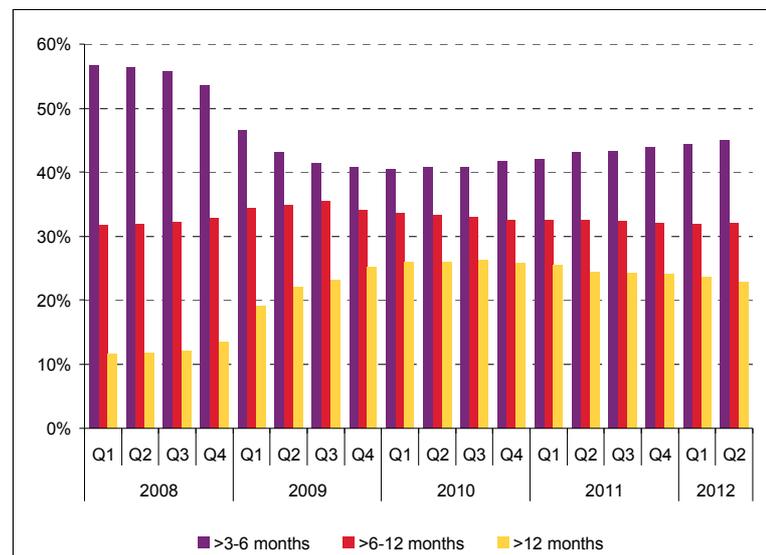
Source: CML, DCLG, FSA MLAR

Exhibit 6.2: Number of cases in arrears and in possession – H1 of 2007, 2010, 2011 and 2012 compared



Source: CML, FSA calculation

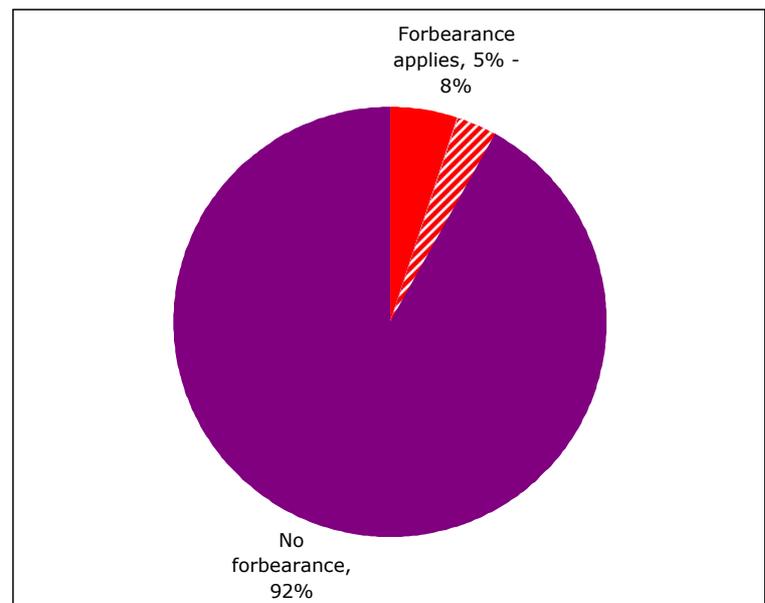
Exhibit 6.3: Structure of arrears, by number of months in arrears



Note: Assuming all arrears >3 months in period = 100%

Source: CML, FSA calculation

- More borrowers are in financial distress than suggested by headline arrears figures.
- This is partly because of lenders' forbearance (of which we only have a partial record) and partly because of the ways in which arrears are defined for reporting purposes.
- We do not have data to compare levels of forbearance today with the 1990s recession. However, the lower interest rate environment combined with the steeper falls in house prices during this downturn mean that lenders have stronger incentives to use forbearance than in the early 1990s.
- Where loans have been or are currently subject to forbearance, e.g. permanent or temporary transfer to interest-only payments, extending the term, reduced payments or payment holidays, the arrears reported to the CML or the FSA may not fully capture the true underlying levels of loan impairment. Forbearance may result in either arrears not showing at all, or at a level lower than they would have been without forbearance.
- The FSA Forbearance Review carried out for the Financial Policy Committee (FPC) suggested that 5%-8% of mortgages could be subject to lenders' forbearance.⁶ Reported arrears figures should, therefore, not be regarded as a complete measure of the underlying levels of loan impairment.

Exhibit 6.4: Extent of lenders' forbearance on residential loans

Note: Forbearance figures are on regulated and non-regulated mortgages.

Source: FSA

⁶ See BoE Financial Stability Report at www.bankofengland.co.uk/publications/fsr/2011/fsrfull1112.pdf

- To illustrate the possible extent of impairment in the mortgage market we use transactional data on arrears, possessions and forbearance that we have collected from a sample of lenders⁷. This transactional data is on regulated mortgages only, so the results we show could be different from those quoted in other sources.
- From the transactional data, we estimate that in March 2012, 7.1% of regulated mortgages had current arrears or payment shortfalls. We also estimate that 12.9% of borrowers that are currently up-to-date with their mortgage payments have had arrears or shortfalls in the past. This means that approximately 20% of outstanding regulated mortgages could have missed payments either currently or in the past.
- Of the 12.9% of mortgages with previous missed payments, we estimate that at least 20% (or 2.6% of all live mortgages) have been subject to some form of forbearance. Under the assumption that these loans would still be in arrears without forbearance, we estimate that the proportion of regulated mortgages with current arrears or payment shortfalls could be as high as 9.7%.
- This is significantly higher than other headline figures suggest (which we show for comparison in Exhibit 6.6). This is because other commonly used definitions of arrears use reporting thresholds that need to be passed for a mortgage to be included in arrears statistics.
- For example, the FSA MLAR uses a 1.5% balance in arrears threshold, and the CML statistics use a 3+ months in arrears

Exhibit 6.5: Mortgage performance cascade: outstanding regulated mortgages

Type of mortgage accounts	Payment shortfall (<2 monthly payments of unknown)	Short to medium-term arrears (>=2 <=6 monthly payments)	Long-term arrears (>6 monthly payments) and possession orders	Repossessions	Total
With record of current missed payments (1)	3.7%	1.3%	1.5%	0.6%	7.1%
With record of past missed payments (2)	5.6%	7.3%			12.9%
including borrowers benefitting from forbearance (3)					2.6%
Total with record of current or past arrears or shortfalls	9.3%	10.1%		0.6%	20.0%
including borrowers with current arrears, shortfalls or forbearance					9.7%
With no record of missed payments					80.0%

Notes:

(1) For accounts with current missed payments, we have total flexibility in banding the data. For accounts with past missed payments, we can only tell reliably if the borrower missed under or over two payments.

(2) Past arrears are understated as some lenders had difficulty reporting this data, particularly on closed mortgages. Closed accounts are the accounts where the borrower has remortgaged, moved, paid off their mortgage, had their house repossessed, or where the account was sold to an entity outside of the sample.

(3) For 2.6% of all live mortgages there is evidence of both past missed mortgage payments and of some form of forbearance. This takes the proportion of live mortgages with missed payments and/or evidenced forbearance to 9.7% of all live accounts.

Source: PSD Performance data 2012

Exhibit 6.6: Mortgage performance as at Q1 2012 based on commonly used measures

Measure	Balances on cases in arrears as % total loan balances	Number of cases in arrears as % total number of loans
MLAR measures (1):		
In arrears >=1.5% balance – regulated mortgages	2.41%	1.81%
of which, in possession	0.16%	0.10%
In arrears >=1.5% balance – non-regulated mortgages	2.89%	2.45%
of which, in possession	0.26%	0.11%
In arrears >=1.5% balance – all mortgages	2.52%	2.02%
of which, in possession	0.19%	0.10%
CML measures (2):		
In arrears >=1.5% balance	-	2.09%
> 3 months in arrears, end period	-	1.96%
Properties taken into possession in period	-	0.09%
Properties in possession at end of period	-	0.12%

Notes:

(1) MLAR figures are calculated on account basis (the same borrower may have several accounts), and are reported on regulated, non-regulated and total residential loans to individuals

(2) CML figures cover first charge mortgage lending only and are on a borrower rather than account basis. They do not correspond with the FSA's MLAR data.

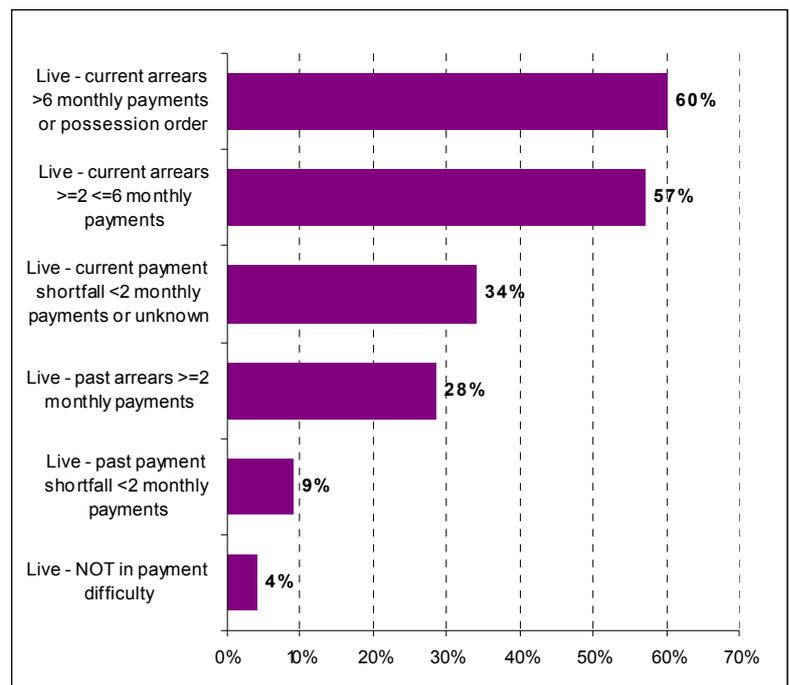
Source: FSA MLAR, CML

⁷ More information on our data and methodology is available in Annex 1 to this data pack.

threshold. The use of thresholds means that some mortgages with missed payments are omitted from the reporting. We estimate that these commonly used definitions of arrears could capture only around a third of all accounts with current missed payments. They also exclude the impact of forbearance.

- As we noted above, from separate research by the FSA for the FPC, 5%-8% of mortgages could be benefiting from forbearance. It is not known if forbearance will help borrowers to overcome a temporary period of hardship before their circumstances improve, or whether arrears are likely to reoccur.
- For regulated mortgages, we estimate that nearly 30% of accounts with a record of current or historic missed mortgage payments could be benefiting from forbearance⁸, which could mask the severity of arrears they would have experienced in the absence of forbearance.
- Around 60% of accounts in current arrears over two months are benefiting.
- A further 4% of borrowers for whom we do not have a record of missed payments have taken steps to reduce their mortgage outgoings by switching to a cheaper repayment method or by extending their mortgage term. Some of these borrowers may have done so for reasons not related to mortgage payment problems. However, some may have done so to avoid developing arrears.

Exhibit 6.7: Provisions of forbearance on regulated mortgages, by type of account performance

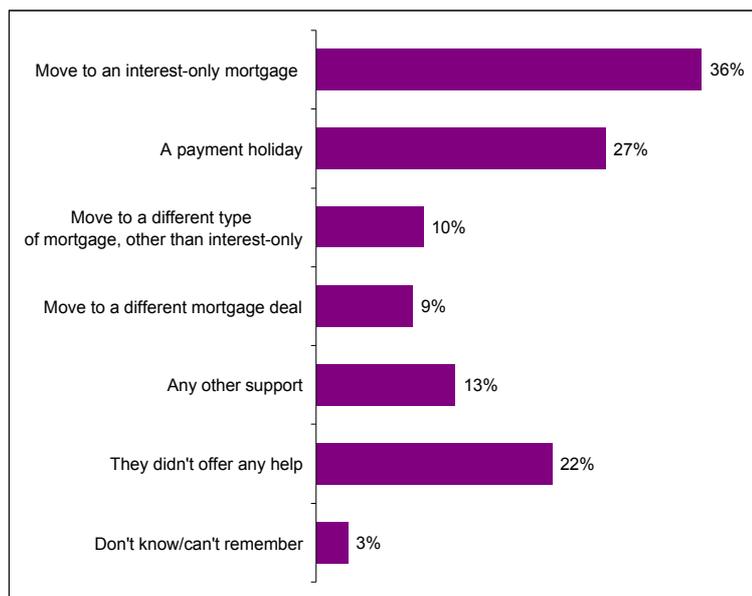


Source: PSD Performance data 2012

⁸ See Annex 1 for the types of forbearance that were included in this estimate.

- According to research by Which?, a switch to an interest-only mortgage, wholly or in part, was the most frequent forbearance option offered to borrowers in difficulty.
- From our data on forbearance provided to borrowers with a record of missed payments, around 30% involved a switch to interest-only wholly or in part.

Exhibit 6.8: Suggestions that lenders made to borrowers who approached them with concerns about mortgage payments, March 2011



Source: Which?

- During the boom, given competitive market pressure and the fact that the prime market was saturated, some banks, building societies and specialist mortgage lenders provided loans to a 'tail' of over-stretched consumers.
- In CP10/16, we discussed our work on risk combinations. We have now updated our analysis with new data. This shows that borrowers with multiple risk characteristics, particularly those with a credit-impaired history, were much more likely to experience arrears and reposessions.

Exhibit 6.9: Risk combinations and mortgage performance

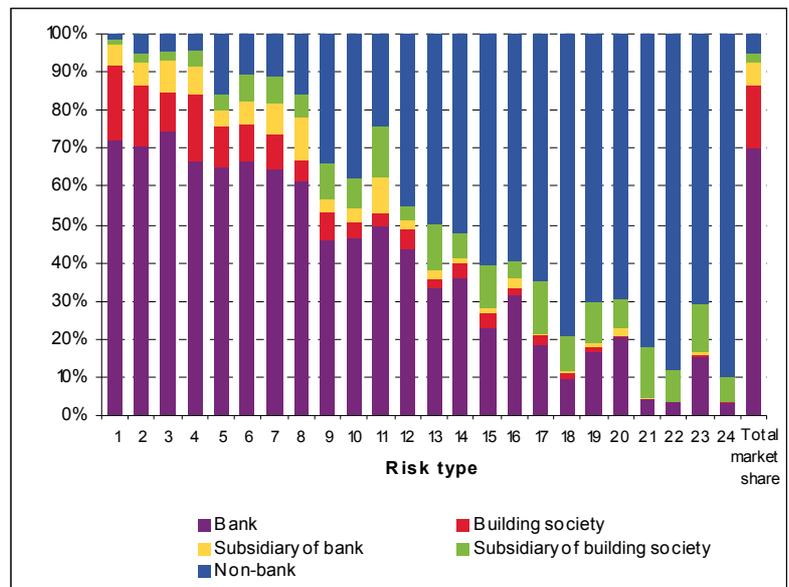
Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of sales	Outstanding mortgages			All sales Total: possessions and possession orders
							Total: any record of missed payments	Total: current missed payments or arrears	Total: current arrears 2+ months	
1	NO	NO	NO	NO	NO	53.5%	13.6%	3.3%	1.1%	0.4%
2	NO	YES	NO	NO	NO	24.1%	22.4%	9.2%	5.0%	2.9%
3	NO	NO	YES	NO	NO	9.1%	22.6%	7.0%	3.1%	1.0%
4	NO	NO	NO	YES	NO	3.1%	23.3%	7.4%	3.0%	0.7%
5	NO	NO	NO	NO	YES	0.6%	33.8%	10.1%	4.6%	2.4%
6	NO	YES	NO	YES	NO	1.2%	36.9%	16.1%	8.2%	4.0%
7	NO	NO	YES	YES	NO	0.5%	38.0%	15.3%	7.6%	1.8%
8	NO	YES	YES	NO	NO	4.2%	38.5%	18.6%	10.1%	5.9%
9	NO	YES	NO	NO	YES	0.2%	44.3%	20.5%	11.3%	8.3%
10	NO	NO	YES	NO	YES	0.1%	44.7%	16.9%	8.6%	4.7%
11	NO	YES	YES	YES	NO	0.2%	56.5%	29.7%	16.6%	7.6%
12	YES	NO	NO	NO	NO	1.0%	60.8%	31.8%	17.2%	7.9%
13	NO	YES	YES	NO	YES	0.0%	61.0%	29.7%	18.5%	12.1%
14	YES	YES	NO	NO	NO	0.8%	67.1%	39.7%	24.9%	15.3%
15	YES	NO	NO	YES	NO	0.2%	68.3%	35.9%	17.1%	6.7%
16	YES	NO	YES	NO	NO	0.4%	75.3%	44.4%	26.0%	12.0%
17	YES	YES	NO	YES	NO	0.2%	76.4%	44.5%	24.5%	13.7%
18	YES	NO	NO	NO	YES	0.1%	79.1%	39.4%	21.8%	13.0%
19	YES	NO	YES	YES	NO	0.1%	81.6%	48.8%	26.8%	9.6%
20	YES	YES	YES	NO	NO	0.3%	81.9%	53.7%	34.6%	21.3%
21	YES	YES	NO	NO	YES	0.0%	82.8%	46.9%	26.2%	21.1%
22	YES	YES	YES	NO	YES	0.0%	85.0%	50.4%	32.5%	26.6%
23	YES	YES	YES	YES	NO	0.1%	86.6%	56.4%	33.2%	17.6%
24	YES	NO	YES	NO	YES	0.0%	86.6%	49.5%	23.8%	13.7%
Total						100.0%	20.0%	7.1%	3.4%	1.8%

Note: The data is on regulated mortgages and is sorted on the basis of the 'any record of payment problems' figure, from the lowest to the highest

Source: PSD Performance data 2012

- Some lenders specialised in higher-risk mortgage products.
- Despite a relatively small market share overall (around 5.3% in April 2005 – June 2012), non-banks⁹ accounted for most sales of higher-risk products.

Exhibit 6.10: Mortgage lenders: market share by risk type

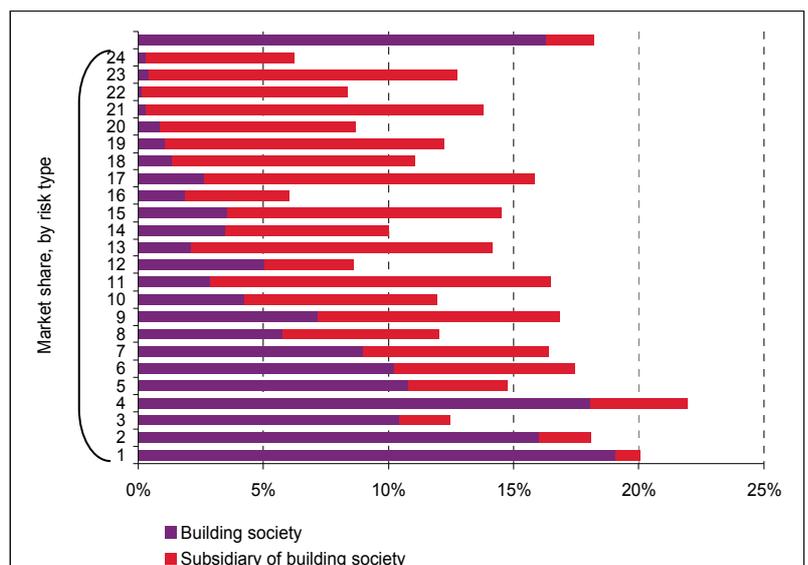


Note: (1) See Exhibit 6.9 for the definitions of risk types; (2) The data is on regulated mortgage sales in April 2005 - June 2012

Source: FSA PSD

- Building societies also targeted higher-risk markets but mainly through their specialist subsidiaries.

Exhibit 6.11: Building societies and their subsidiaries: market share by risk type



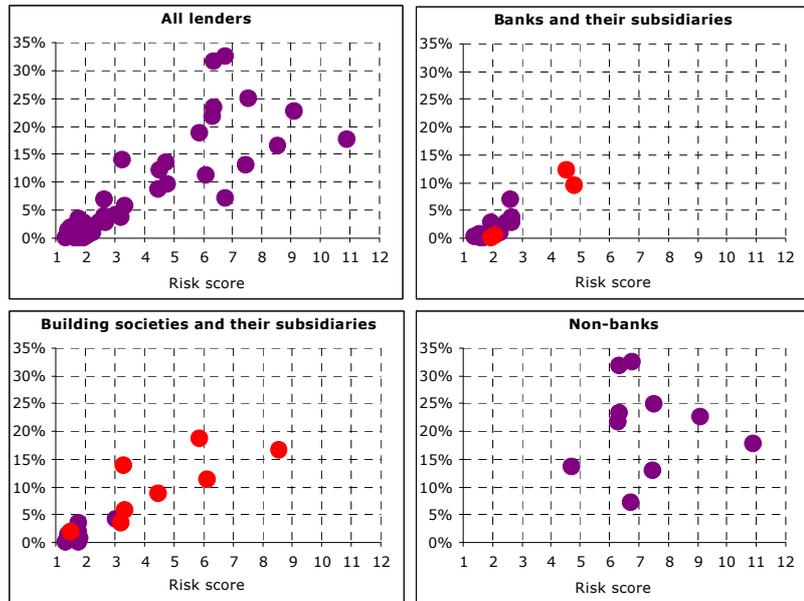
Note: (1) See Exhibit 6.9 for the definitions of risk types; (2) The data is on regulated mortgage sales in April 2005 - June 2012

Source: FSA PSD

⁹ See Annex 1 for the definition of non-banks used in this paper.

- Some lenders took higher risks than others and have experienced much higher arrears rates.
- However, the level of arrears cannot always be explained by the risks lenders were running. Poor underwriting standards were also a factor. Some lenders performed more poorly than other lenders taking the same level of risk.
- Overall, building societies and banks ran the lowest risks and had the lowest level of arrears, while non-banks and subsidiaries of building societies ran the highest risks and experienced the highest level of arrears.

Exhibit 6.12: Relationship between level of mortgage risk and 2+ months current arrears, by type of lender

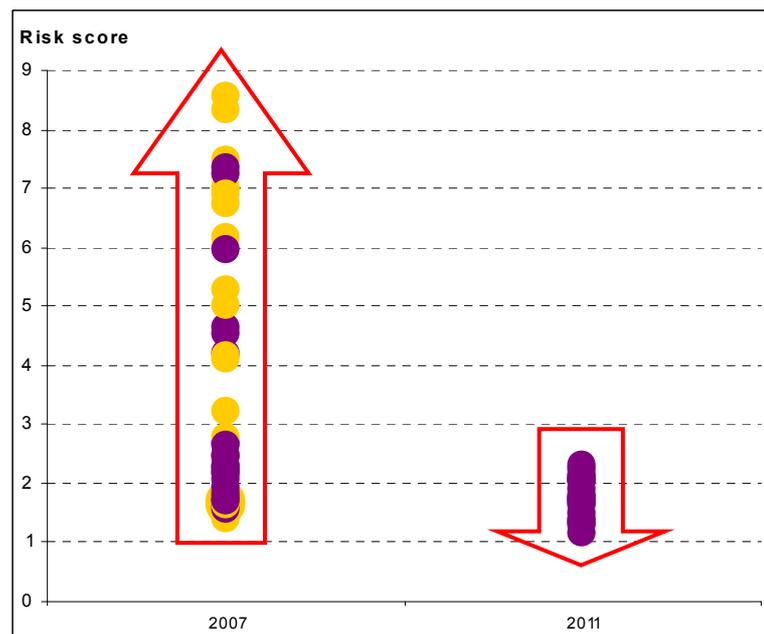


Note: (1) The data is on regulated mortgages that were outstanding as at December 2010 – December 2011 (2) We explain in Annex 1 how we worked out the risk scores; (3) y-axis show proportion of mortgages in current arrears of 2+ months; (4) red dots represent subsidiaries.

Source: PSD Performance data 2012

- The risk profile of lending has changed significantly between 2007 and 2011.
- Many lenders who were active in 2007 have left the market or had to merge with other lenders. The risk appetite has significantly reduced as well.

Exhibit 6.13: Risk profile of new mortgage lending in 2007 and 2011, by lender

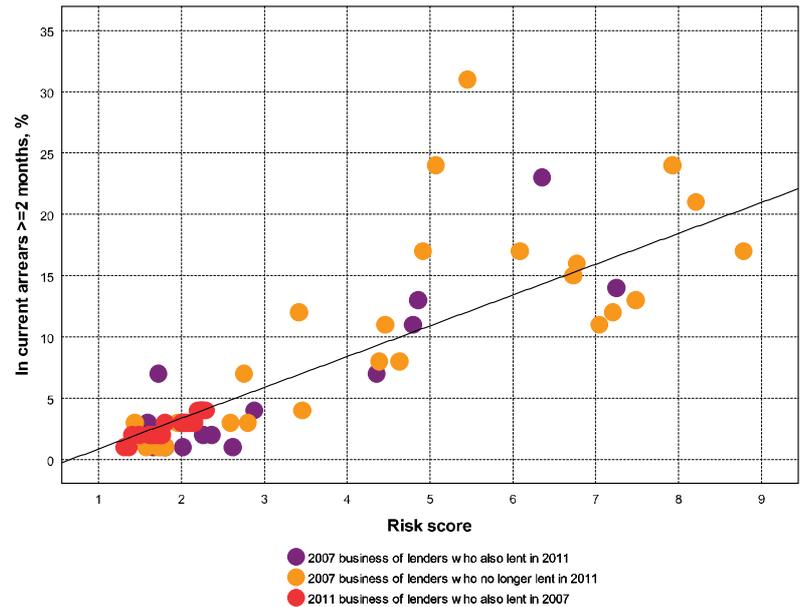


Note: Lenders shown as purple dots lent both in 2007 and 2011. Lenders shown as yellow dots stopped new lending, left the market or merged with other lenders

Source: PSD Performance data 2012

- Following the market downturn, lenders have considerably tightened their criteria. For lenders that lent both in 2007 and 2011, we observe a significant reduction in risk, which is likely to lead to a considerable improvement in performance, as illustrated.

Exhibit 6.14: Change in lending risks and arrears from 2007 to 2011

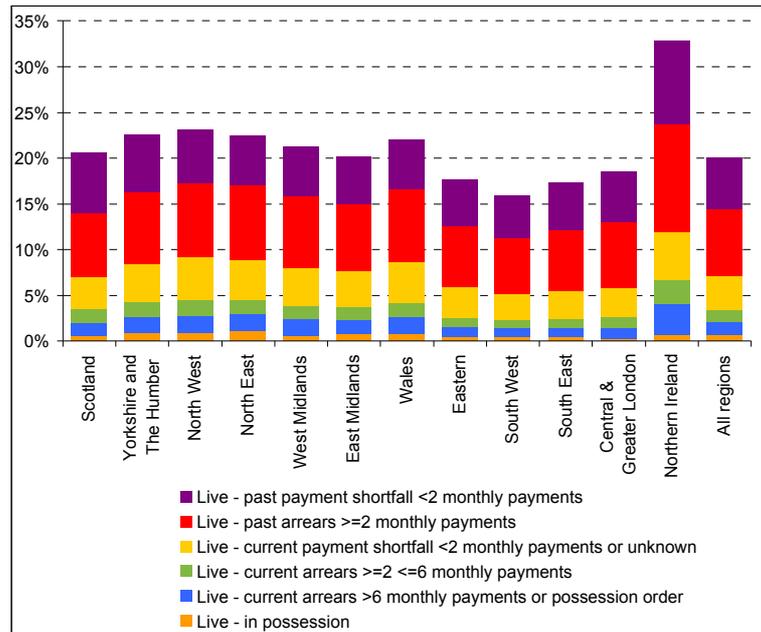


Note: This Exhibit is based on the mortgages sold in 2007 and 2011 that were still outstanding in March 2012. For mortgages sold in 2007, the Exhibit shows observed risk score at origination and observed performance as at March 2012. For mortgages sold in 2011, we also show observed risk scores at origination. However, as these mortgages are relatively new and did not have sufficient time to develop performance problems fully, we did not use their observed arrears. Instead, we have made a forecast of how these mortgages were expected to perform in March 2015, so four years on from origination. In order to do that, we have used a formula that describes the linear relationship between risk scores of mortgages sold in 2007 and their subsequent performance in March 2012 for the lenders who lent both in 2007 and in 2011.

Source: PSD Performance data 2012

- Regionally, there are considerable differences in the proportion of mortgages with payment problems.
- Overall, a higher proportion of borrowers experienced arrears and payment shortfalls in the northern and western regions than in the southern and eastern regions.

Exhibit 6.15: Mortgage performance, by region

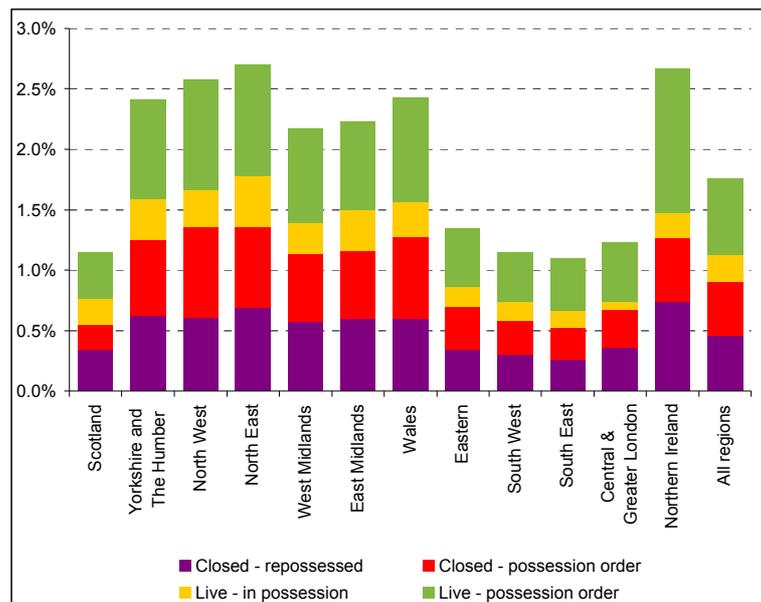


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- A similar situation was observed for repossessions.
- A higher proportion of those borrowers who had taken out mortgages since April 2005 had their homes repossessed or had a possession order secured against their homes in the northern (apart from Scotland) and western regions than in the southern and eastern regions.

Exhibit 6.16: Mortgage repossessions, by region

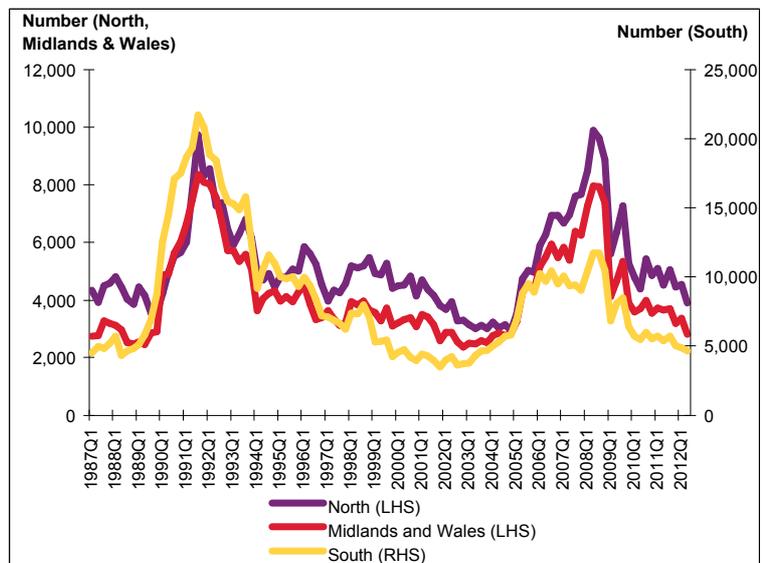


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- While data on mortgage arrears by region is not available back to the early 1990s, there is consistent data on mortgage possession orders by region for England and Wales.
- While the peak in the number of possession orders in the period since 2007 is lower than in the corresponding period in the 1990s, this is due to the lower levels of possession orders made in the southern regions of England.
- Possession orders made in northerly areas are at least as high as those experienced in the 1990s.

Exhibit 6.17: Possession orders by region, long-term trend

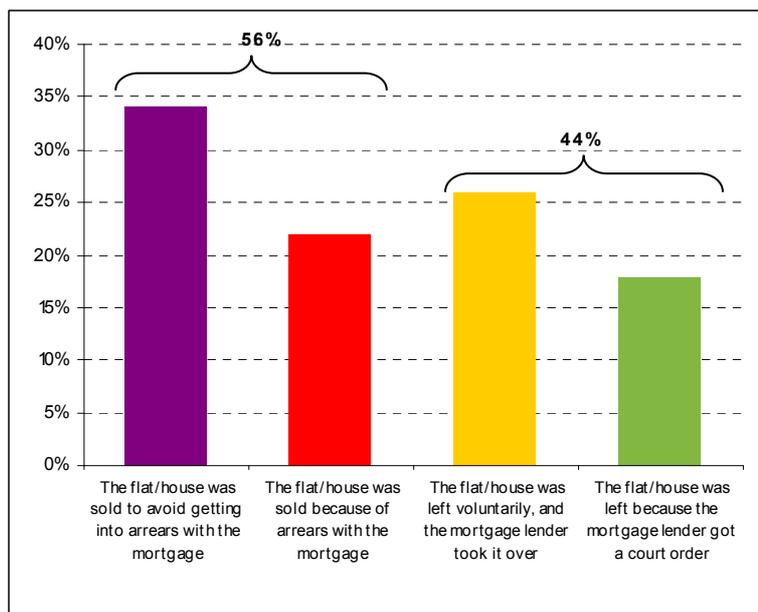


Note: In this Exhibit, the south is defined as London, South East, South West, East of England; Midlands is East Midlands and West Midlands; and the North is North East, North West and Yorkshire and Humberside.

Source: Ministry of Justice

- The statistics on repossessions could understate the numbers of people who lose their homes because they can't keep up with their mortgage payments.
- Survey data suggests that fewer than half of all people who lost their homes (44%) did so because they were repossessed by lenders.
- Over half (56%) sell their homes voluntarily to avoid going into arrears or to pay off arrears.

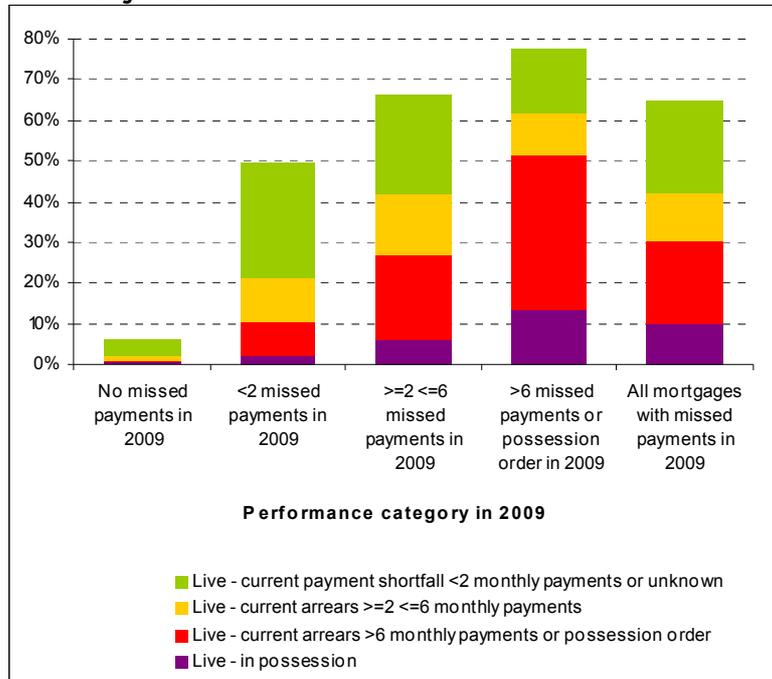
Exhibit 6.18: Reasons why homes are given up



Source: Survey of English Housing, 1993-2007

- Not all borrowers in arrears recover and get back on track with their mortgage payments – 65% of borrowers with outstanding mortgages for whom we had a record of current missed payments in August 2009 again had missed payments reported in March 2012.
- Of mortgages with severe arrears of over six months, 78% still had arrears or shortfalls in March 2012.
- Here, we have not considered the impact of forbearance.

Exhibit 6.19: Mortgages that were in arrears in August 2009 – how many are still in arrears in 2012?



Note: (1) 2012 performance data reflects arrears position as at March 2012, as reported by the sample of lenders. The data shows performance of mortgages sold between April 2005 and December 2011 that were outstanding on the date of reporting. (2) Around 27% of accounts with missed payments in August 2009 are now closed, of which over 60% were repossessed. These accounts are not shown on the Exhibit above.

Source: PSD Performance data 2009 and 2012

- For many borrowers arrears could worsen over time and end in repossession.
- Nearly 30% of borrowers who were in arrears in August 2009 either had their property repossessed or had a possession order secured against their property.
- A further 9% may have sold their home voluntarily to avoid repossession.
- We estimate that over half of borrowers who were in severe arrears of 6+ months in August 2009 may have lost their home by March 2012.
- Even those borrowers who had shortfalls under two months in August 2009, could have subsequently developed serious problems, leading to up to quarter losing their home to a repossession or to a voluntary sale.

Exhibit 6.20: Outcomes for mortgages that were in arrears in August 2009 - measured at March 2012



Note: 'Closed other' category includes mortgages that were paid off, i.e. when the borrower sold property, moved house or paid off mortgage to become a mortgage-free owner-occupier.

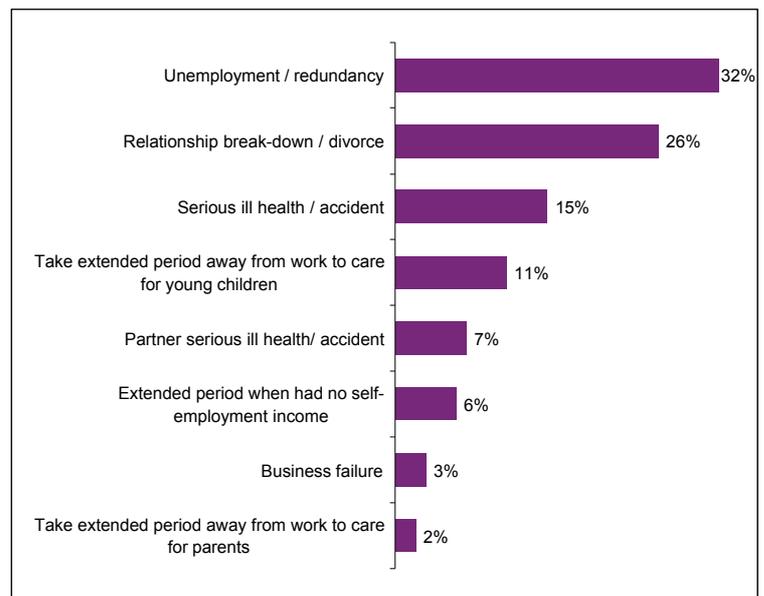
Source: PSD Performance data 2009 and 2012

7

Causes of payment problems

- For many borrowers, a mortgage is a long-term financial commitment that can typically last for up to 25 years or even for longer.
- Over the mortgage term, some borrowers may experience life events that could lead to a reduction in their income or to an increase in expenditure. For example, 32% of mortgage borrowers who took part in the Policis survey said that at some point they had been made unemployed or redundant; 26% had experienced a relationship breakdown; and 15% had been seriously ill or had an accident.
- Depending on their severity and duration, some life events can affect borrowers' ability to make mortgage payments – indeed some borrowers say that unemployment and other life events caused mortgage payment problems (see Exhibit 7.11).
- While life events do trigger arrears for some borrowers, the true causes could be deeper: many mortgage borrowers who are overleveraged and financially overstretched would not be able to cope financially even with life events with a short-term impact.

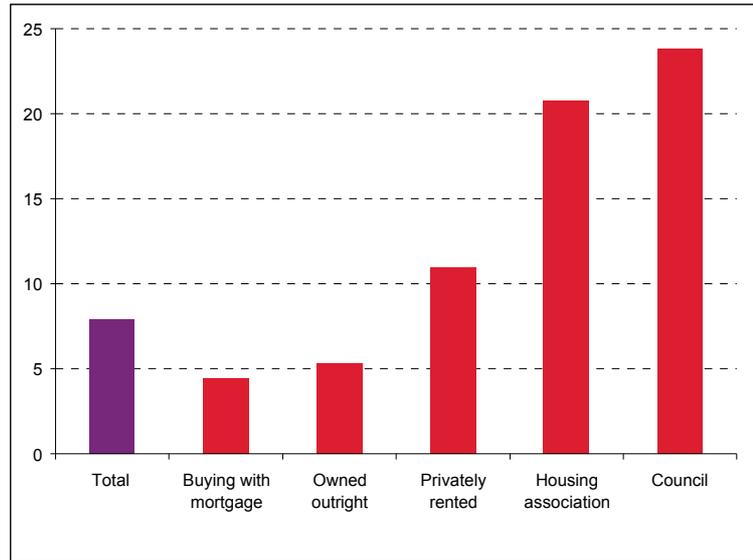
Exhibit 7.1: Proportion of borrowers who have ever experienced adverse life events and income shocks



Source: Policis

- Unemployment is the most common life event that may affect mortgage borrowers and in most cases means immediate reduction in household income.
- Although unemployment among mortgage borrowers is less common than among the general population, as of Q2 2012, 4.4% of people in households with a mortgage were unemployed.

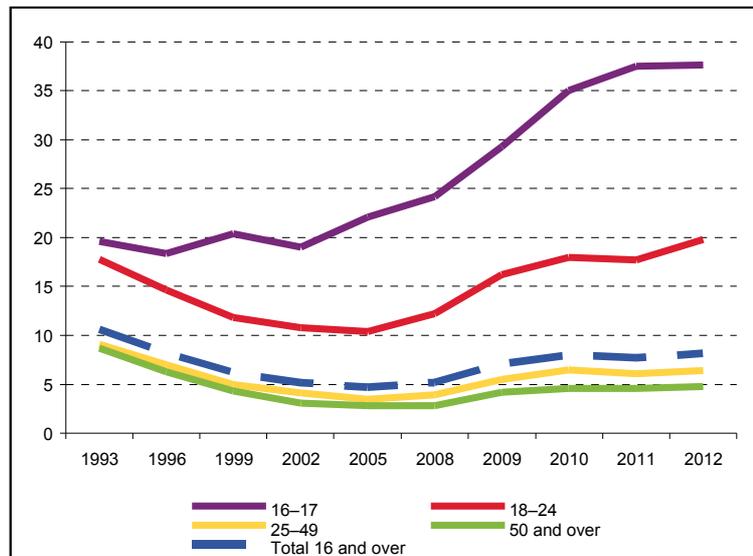
Exhibit 7.2: Unemployment rate by housing tenure, Q2 2012



Source: Labour Force Survey

- The unemployment figures for mortgage borrowers noted above may appear low in comparison with headline figures reported in the press.
- In part, this is because the recent increase in unemployment was mainly driven by youth unemployment (16-24 year olds) and most mortgage borrowers are older.

Exhibit 7.3: Unemployment rates, by age



Note: The data is from Q1 of each year and seasonally adjusted

Source: ONS

- Unemployment and other adverse life events undoubtedly trigger payment problems for some borrowers. But is this the main cause of arrears or are arrears caused by financial overstretch?
- In the absence of individual-level data we cannot answer this question precisely. However, we can look at the data on the financial position of mortgage borrowers that is available from various sources.
- A BoE survey suggests that 13% of mortgage borrowers do not have enough savings to cover even one mortgage payment. 26% do not have enough savings to cover three monthly payments.

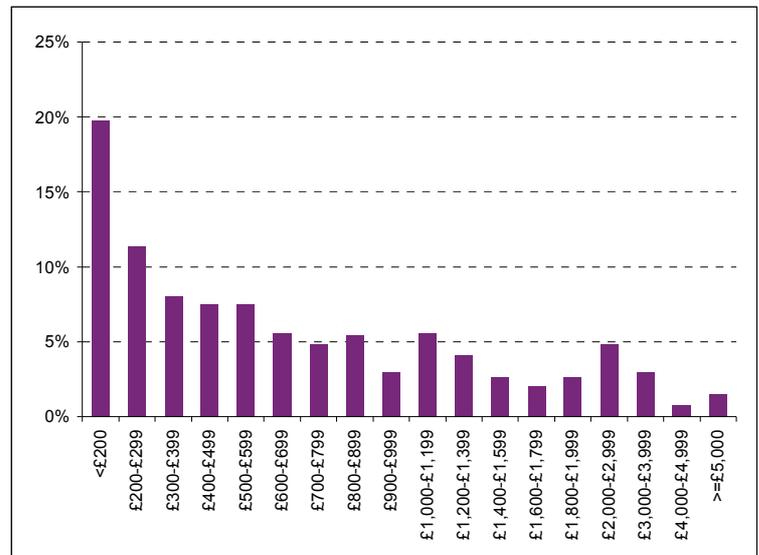
Exhibit 7.4: Amount of savings available to mortgage borrowers in relation to their monthly mortgage payments



Source: BoE / NMG survey 'The financial position of UK households' 2011, FSA analysis

- Moreover, around 20% of mortgage borrowers have less than £200 to live on after paying their housing bills and mortgage.
- This suggests that many supplement their income with credit.

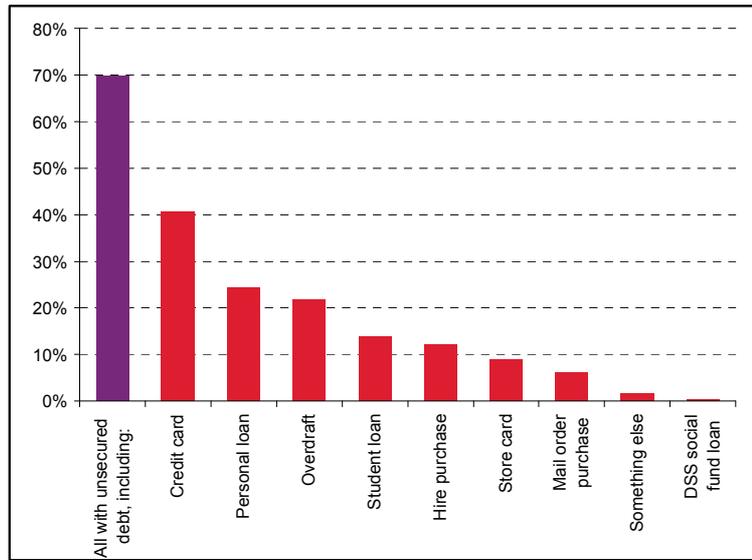
Exhibit 7.5: Mortgage borrowers: amount of money left after housing bills and mortgage, per month



Source: BoE / NMG survey 'The financial position of UK households' 2011, FSA analysis

- Indeed, it follows from the BoE / NMG survey, that 70% of mortgage borrowers have unsecured debt.

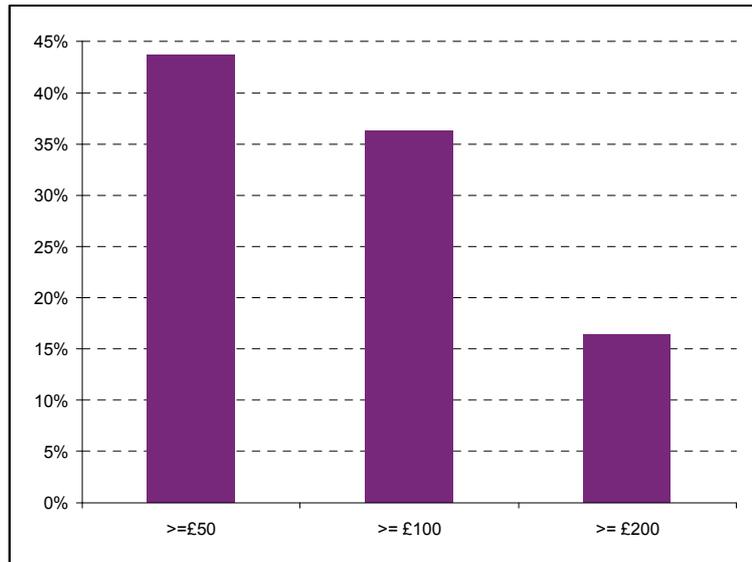
Exhibit 7.6: Mortgage borrowers with unsecured debt



Source: BoE / NMG survey ‘The financial position of UK households’ 2011, FSA analysis

- Servicing unsecured debt can take a non-trivial amount of mortgage borrowers’ income. For example, 36% of mortgage borrowers with unsecured debts are paying more than £100 each month towards their unsecured debts.
- Unsurprisingly, many mortgage borrowers struggle to pay their bills and credit commitments, which we have illustrated in Chapter 3 of this data pack. Exhibit 3.7 shows that, despite low interest rates, many mortgage borrowers are financially overstretched and are finding it increasingly difficult to meet their ongoing financial commitments.

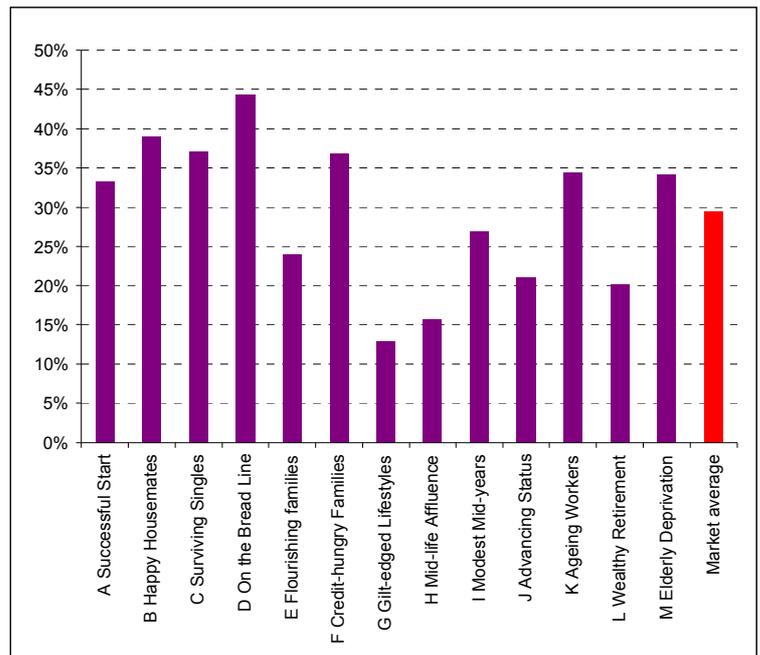
Exhibit 7.7: Mortgage borrowers with unsecured debt: how much they spend each month on unsecured debt payments



Source: BoE / NMG survey ‘The financial position of UK households’ 2011, FSA analysis

- Some borrowers are more over-indebted than others. Here, we use Experian Financial Strategy Segments (FSS) categories to illustrate this.
- Although we do not have data on unsecured debts, our analysis of the data on mortgages shows that some types of borrowers are more likely than others to be highly leveraged (as illustrated here by high LTV mortgage borrowing).
- For example, in 2005-2011, 44% of borrowers that Experian categorises as ‘on the breadline’ took out mortgages with LTVs in excess of 80%. The market average for 80%+ LTV borrowing in this period was 29%.

Exhibit 7.8: Sales of 80%+ LTV mortgages within geo-demographic group

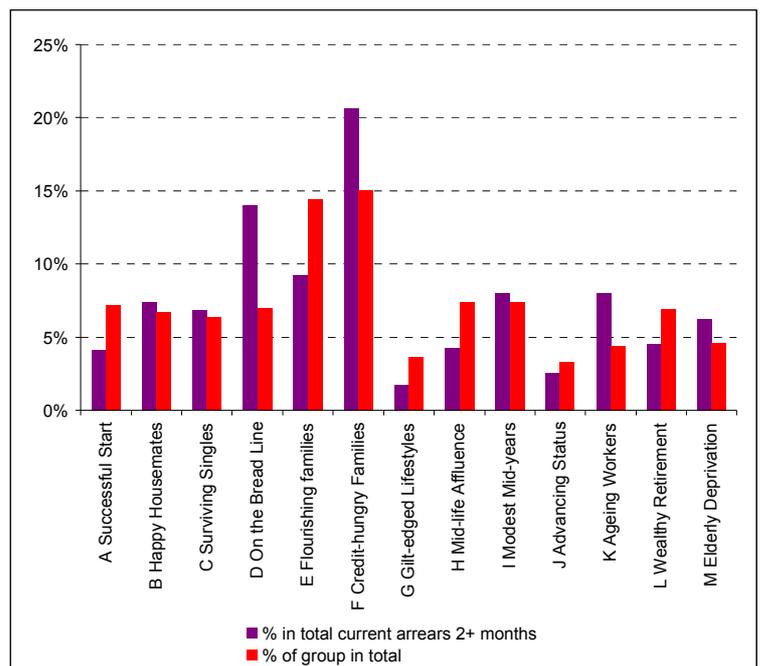


Note: Regulated mortgages sold in April 2005 - December 2011

Source: FSA PSD, Experian

- Unsurprisingly, mortgage borrowers who are more likely to be over-indebted are also more likely to be in arrears or have their homes repossessed.
- For example, consumer categories that Experian classifies as ‘credit-hungry’, ‘on the breadline’, ‘ageing workers’ and ‘elderly deprivation’, account for 31% of all households with a mortgage but for 49% of current arrears cases in excess of two months.

Exhibit 7.9: Arrears of 2+ months: geo-demographic distribution

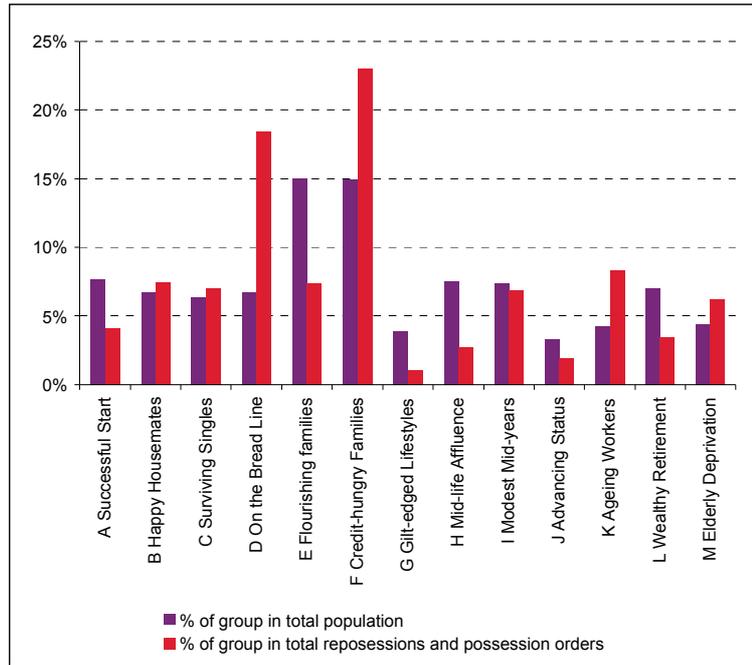


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012, Experian

- Similarly, the same borrower groups account for 56% of all repossessions.

Exhibit 7.10: Repossessions on mortgages sold in April 2005 - December 2011: geo-demographic distribution

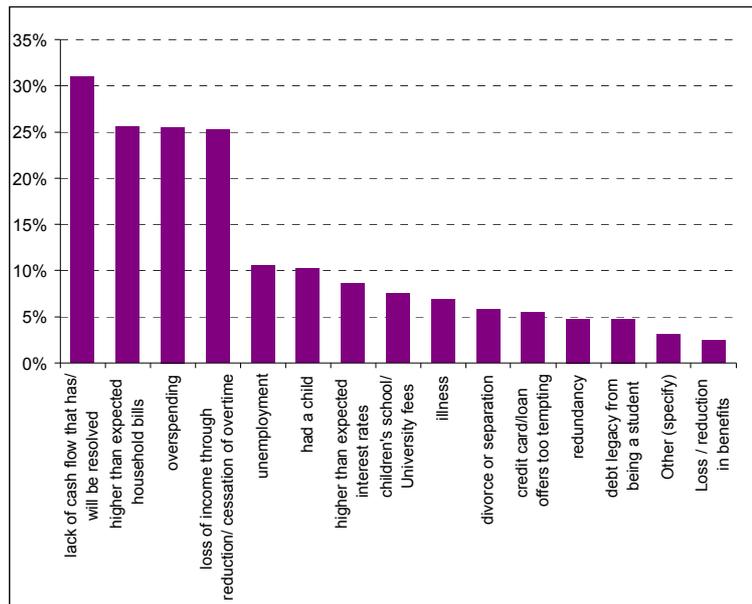


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012, Experian

- The most frequently quoted reasons for difficulties with mortgage payments, in the BoE/NMG survey, are: lack of cash flow; higher than expected household bills; overspending; and loss of income through reduction/stopping of overtime. These were quoted by over 25% of all struggling respondents.
- Interestingly, a much smaller proportion of mortgage borrowers (less than 10%) said that life events, such as unemployment, illness or having a child were the cause of their hardship.

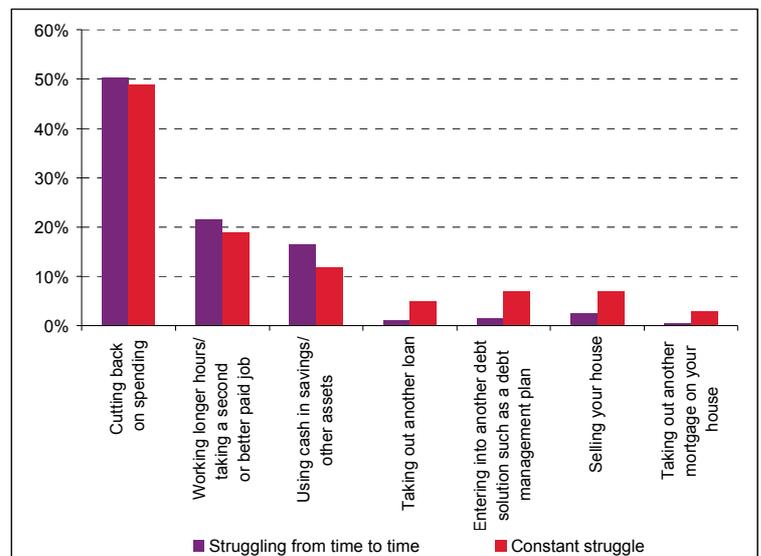
Exhibit 7.11: Mortgage borrowers: reasons for difficulties in keeping up with bills and/or credit commitments



Source: BoE / NMG survey 'The financial position of UK households' 2010, FSA analysis

- To resolve the situation, many proposed to cut back on spending or to get extra income. We do not know whether they were in fact able to do this.
- Worryingly, some would like to take another loan on mortgage to help with payments.

Exhibit 7.12: Mortgage borrowers: what actions, if any, are you taking to resolve the difficulty you have in keeping up with bill and/or credit commitments?



Source: BoE / NMG survey 'The financial position of UK households' 2011, FSA analysis

PART III

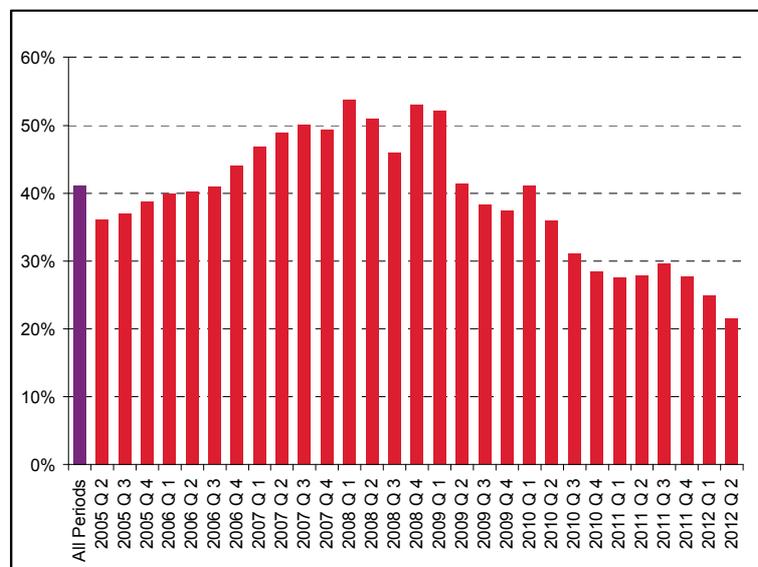
Responsible lending

8

Income verification

- At the peak of the market, over half of all mortgages were granted with no verification of income...

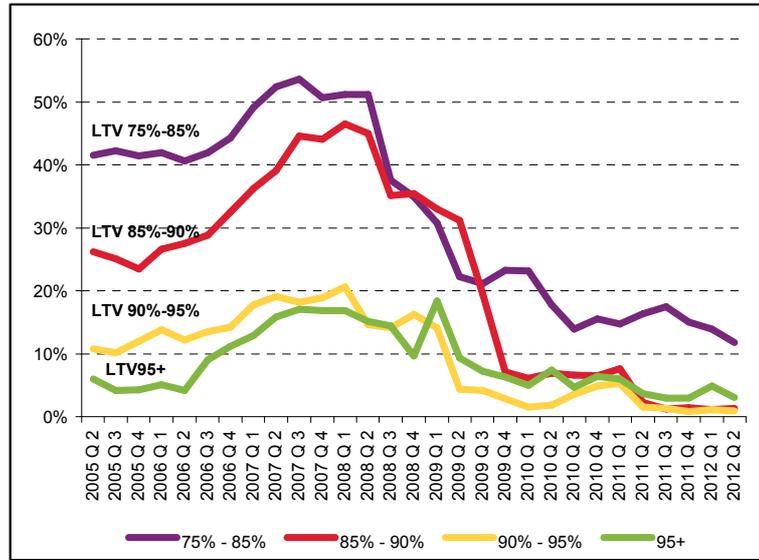
Exhibit 8.1: Proportion of mortgages where income was not verified



Source: FSA PSD

- ...including a significant proportion of mortgages at higher-LTV bands...

Exhibit 8.2: Higher-LTV mortgages where income was not verified



Source: FSA PSD

- ...and to higher-risk borrower types.

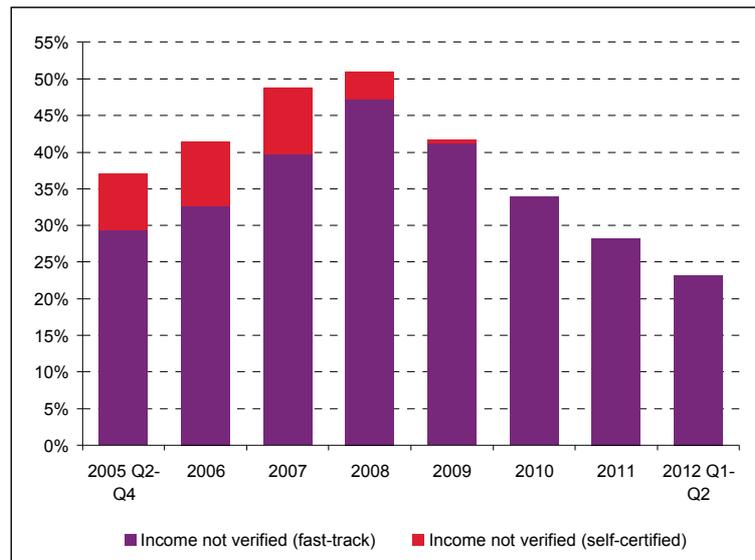
Exhibit 8.3: Mortgage sales where income was not verified, by risk type

Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	Income not verified
1	NO	NO	NO	NO	NO	48%
2	NO	YES	NO	NO	NO	22%
3	NO	NO	YES	NO	NO	58%
4	NO	NO	NO	YES	NO	51%
5	NO	NO	NO	NO	YES	46%
6	NO	YES	NO	YES	NO	36%
7	NO	NO	YES	YES	NO	69%
8	NO	YES	YES	NO	NO	58%
9	NO	YES	NO	NO	YES	20%
10	NO	NO	YES	NO	YES	70%
11	NO	YES	YES	YES	NO	71%
12	YES	NO	NO	NO	NO	37%
13	NO	YES	YES	NO	YES	59%
14	YES	YES	NO	NO	NO	30%
15	YES	NO	NO	YES	NO	43%
16	YES	NO	YES	NO	NO	84%
17	YES	YES	NO	YES	NO	36%
18	YES	NO	NO	NO	YES	36%
19	YES	NO	YES	YES	NO	88%
20	YES	YES	YES	NO	NO	76%
21	YES	YES	NO	NO	YES	26%
22	YES	YES	YES	NO	YES	78%
23	YES	YES	YES	YES	NO	79%
24	YES	NO	YES	NO	YES	84%
Total						43%

Source: PSD Performance data 2012

- There were two types of non-income-verified mortgages in the market: fast-tracked and self-certified.
- Fast-tracking means that the lender does not necessarily look at income documentation as the loan is considered low risk. Self-certification means that income documentation is not required as a product feature.
- We estimate that most non-income-verified mortgages were fast-tracked. However, over time, market practice meant that the line between fast-tracking and self-certification became blurred.

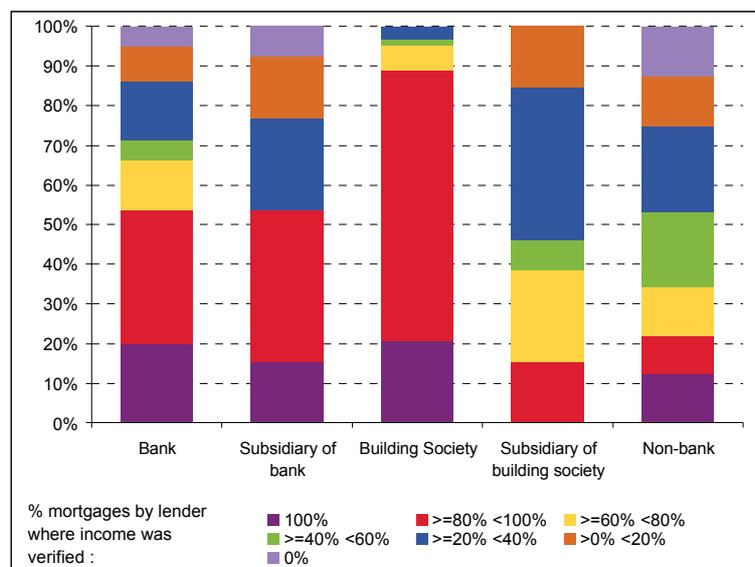
Exhibit 8.4: Mortgage sales where income was not verified, by type of non-verification



Source: FSA estimates based on PSD

- Although non-verification of borrowers' incomes was a widespread market practice, some lenders, mainly smaller building societies but also some large banks, verified income in all or in most cases.
- We estimate that nearly 60% of lenders active in the market in 2005-2012 verified income in over 80% of all mortgage sales - this includes 90% of building societies and 55% of banks. Nearly 50% of building societies and over 20% of banks verified income in every single case.

Exhibit 8.5: Proportion of lenders, by type, that verified income

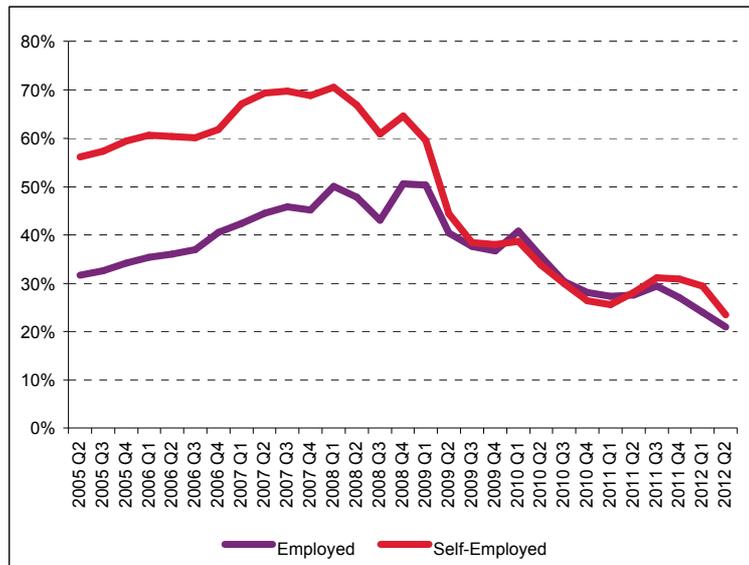


Note: Regulated mortgage sales in April 2005 - June 2012

Source: FSA PSD

- Before the market downturn, self-employed borrowers were much more likely than employed borrowers to have non-income-verified mortgages. However, this changed following the post-crisis tightening of lending criteria.

Exhibit 8.6: Mortgage sales with non-verified income, by employment status



Source: FSA PSD

- Proportionally, self-employed borrowers were much more likely than employed to self-certify their income.

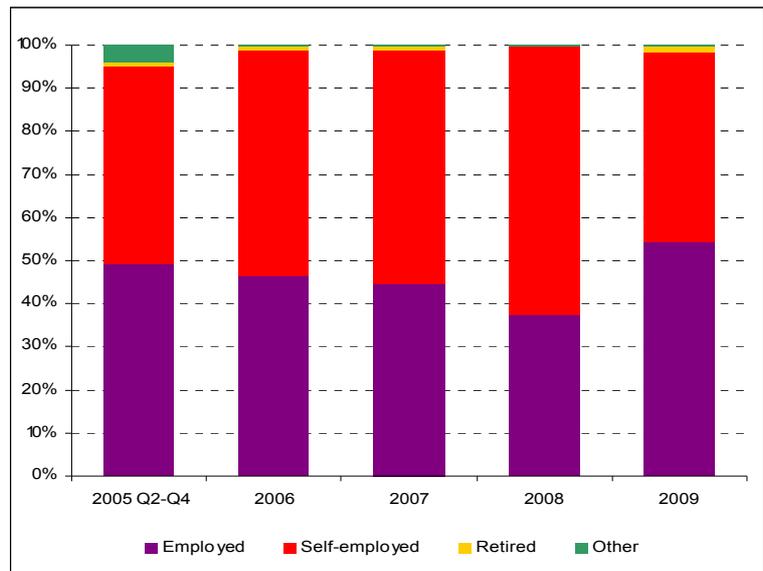
Exhibit 8.7: Self-certification, by employment status: trend over time



Source: PSD Performance data 2011, FSA PSD

- However, overall, nearly half of all self-certified mortgages were sold to employed borrowers¹⁰ – the customer type for which these mortgages were never intended.

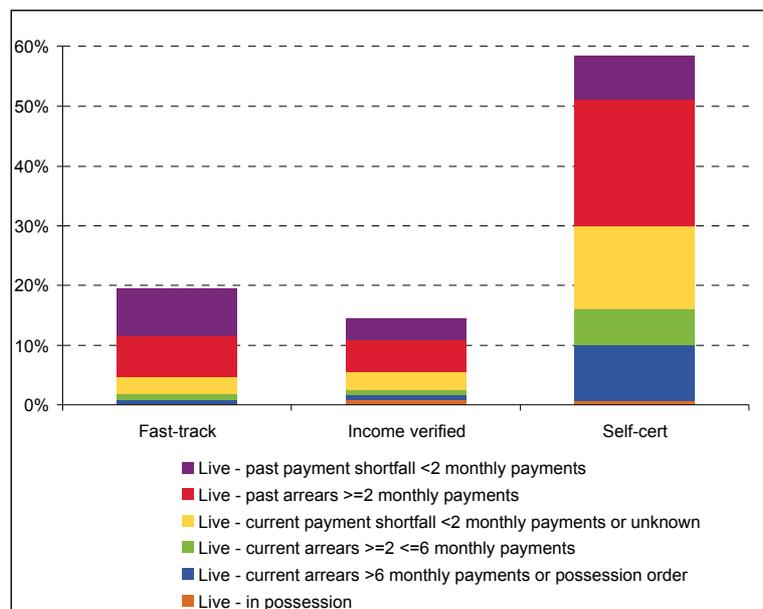
Exhibit 8.8: Structure of self-certified mortgage sales, by employment status



Source: PSD Performance data 2011

- In CP10/16 we reported that fast-tracked mortgages performed better than mortgages where income was verified.
- The new data we have collected on mortgages that were outstanding in March 2012 showed that, overall, arrears and payment shortfalls on fast-tracked mortgages were somewhat higher than on mortgages where income was verified.¹¹ Self-certified mortgages perform much worse.
- If historic arrears and payment problems are excluded from the analysis, fast-tracked mortgages would appear to perform somewhat better than mortgages where income was verified. This is because most lenders apply a set of criteria to identify mortgages that are eligible for fast-tracking, such as an LTV.

Exhibit 8.9: Mortgage performance, by type of income verification



Note: This Exhibit shows performance of mortgages sold in April 2005 – December 2011 that were outstanding as at March 2012 when performance was measured.

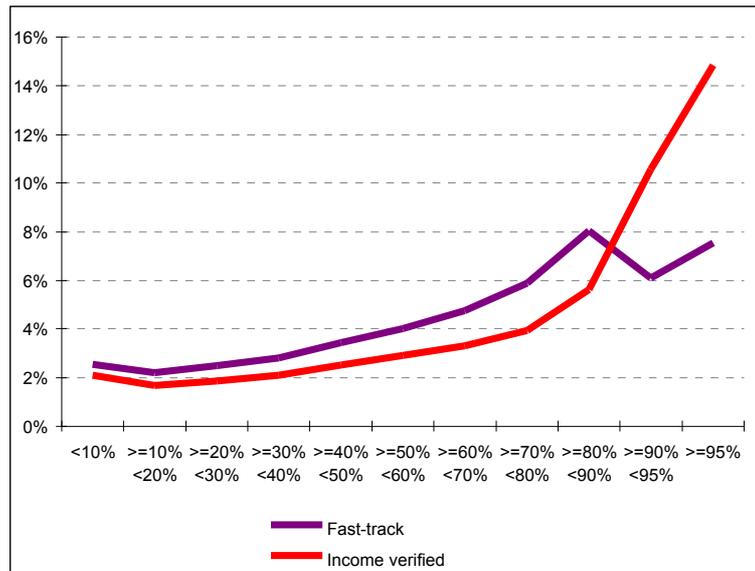
Source: PSD Performance data 2012

¹⁰ A small proportion of employed borrowers could have had multiple incomes or varying incomes, so could have used self-certification for these reasons.

¹¹ The differences we observe is due to the data on past arrears and payment problems that was not available to us for CP10/16 analysis. Some lenders had difficulty reporting past performance problems and our data is incomplete. So the differences in performance of fast-track and income-verified mortgages could be due to changes in our sample and in the methodology of data collection. They do not constitute a time trend.

- When we look at performance of mortgages by type of income verification and by LTV, it seems that fast-tracked mortgages in the same LTV band do not perform any better than mortgages where income was verified. The only exception is high LTV mortgages – however, the difference in performance at high LTV bands could be due to smaller sample sizes of fast-tracked mortgages.

Exhibit 8.10: Current arrears and shortfalls, by type of income verification and LTV

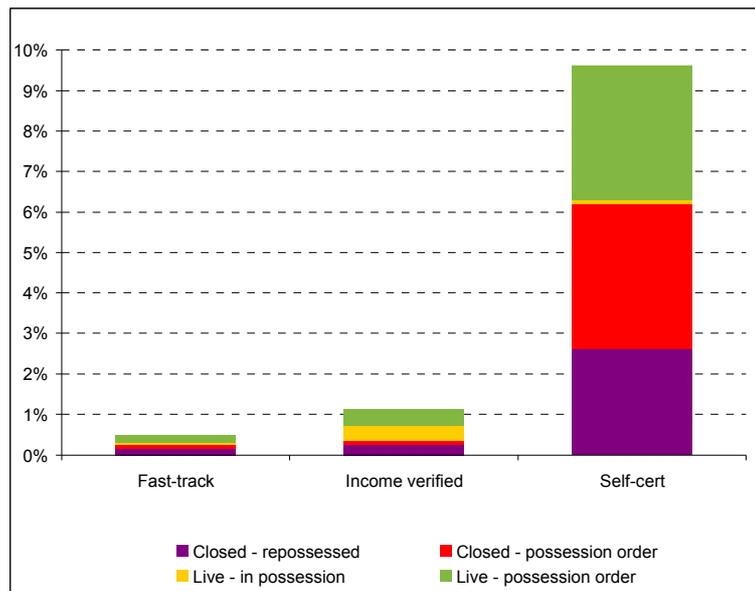


Note: This Exhibit shows current arrears and shortfalls on mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Borrowers whose mortgages were fast-tracked were considerably less likely to have their homes repossessed.

Exhibit 8.11: Mortgage repossessions, by type of income verification

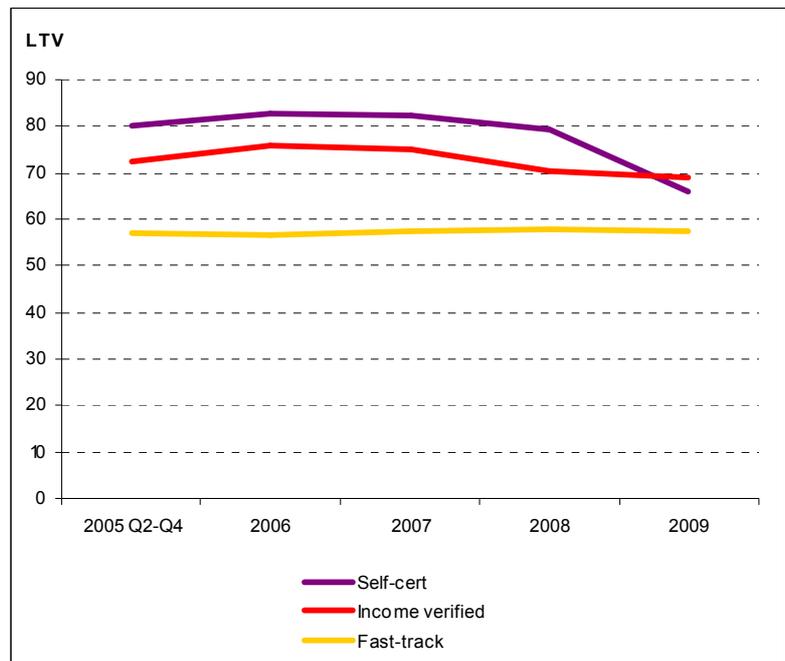


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- This is because fast-tracked mortgages generally have lower LTVs.
- Lenders could be more willing to show forbearance on mortgages where their security is not at risk.

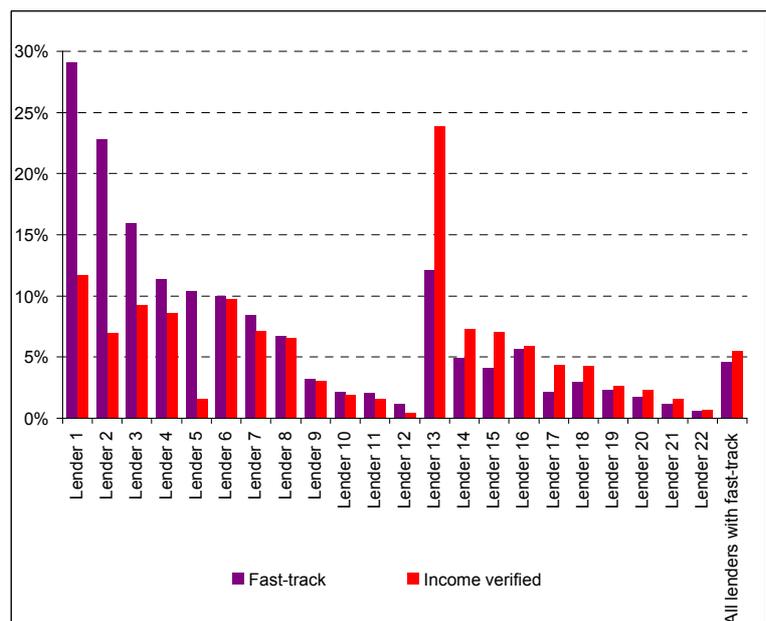
Exhibit 8.12: Median LTV at mortgage origination, by type of income verification



Source: PSD Performance data 2011

- When looking at current payment shortfalls and arrears, for 12 out of 22 lenders who operated a fast-track process, their fast-tracked mortgages performed worse than mortgages where income was verified; for some lenders, considerably worse.

Exhibit 8.13: Proportion of mortgages with current payment shortfalls or arrears: fast-tracked and income verified, by lender



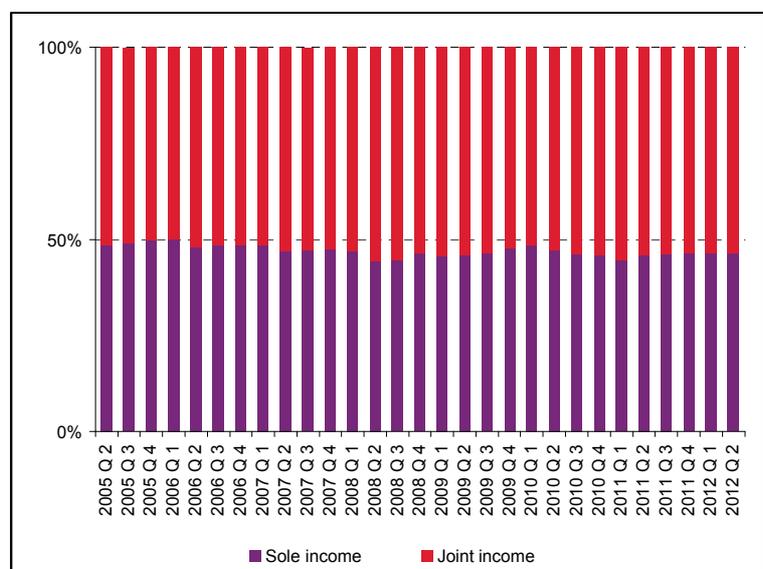
Source: PSD Performance data 2012

9

Income and expenditure

- Consumers can apply for a mortgage on their own or together with someone else (e.g. with their partner).
- Sole income means that the mortgage is backed by just one income - this could mean a single-person household or a family where just one adult works.
- Joint income means that there are two or more applicants.
- A slightly higher proportion of borrowers obtain mortgages on joint incomes than on sole incomes.

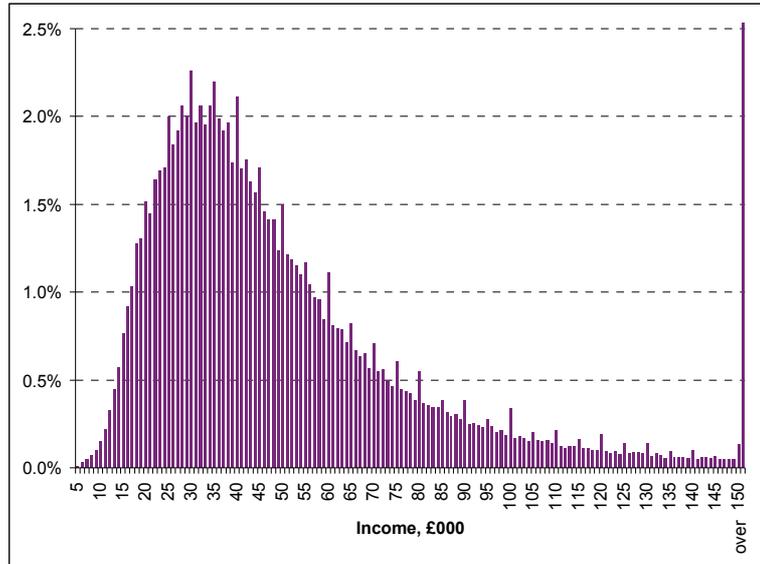
Exhibit 9.1: Mortgage sales, sole or joint income



Source: FSA PSD

- The incomes of mortgage borrowers vary greatly – from the relatively low to the very high.

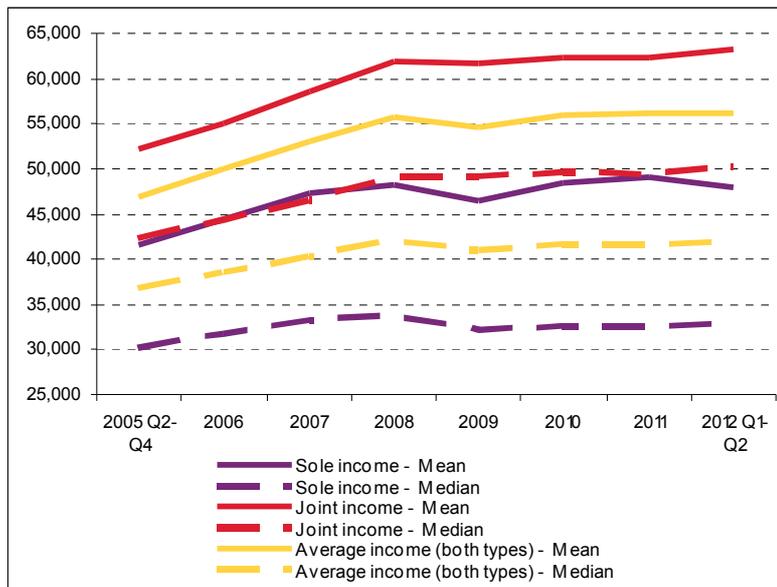
Exhibit 9.2: Gross annual household incomes of mortgage borrowers: distribution in January – June 2012



Source: FSA PSD

- In 2011, the average sole income stood at £49,000 and the average joint income stood at £62,000.

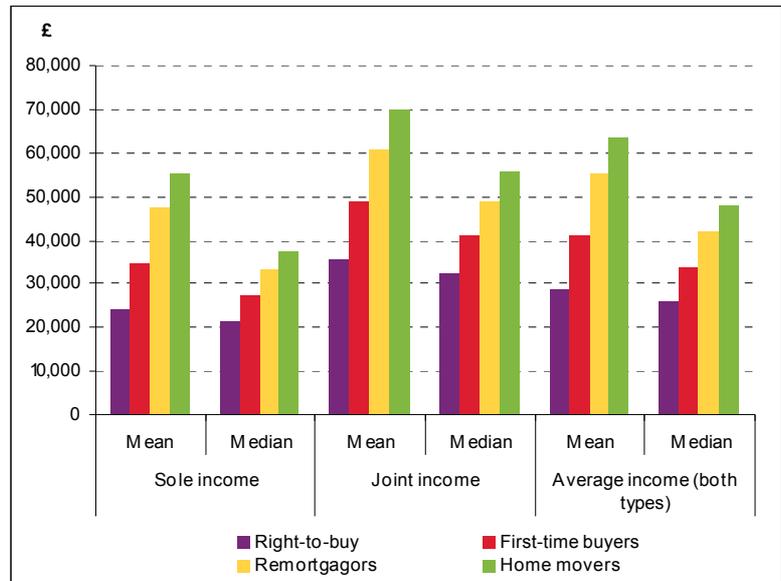
Exhibit 9.3: Average gross annual incomes of mortgage borrowers



Source: FSA PSD

- On average, RTB borrowers and FTBs have lower incomes and remortgagors and home movers have higher incomes.

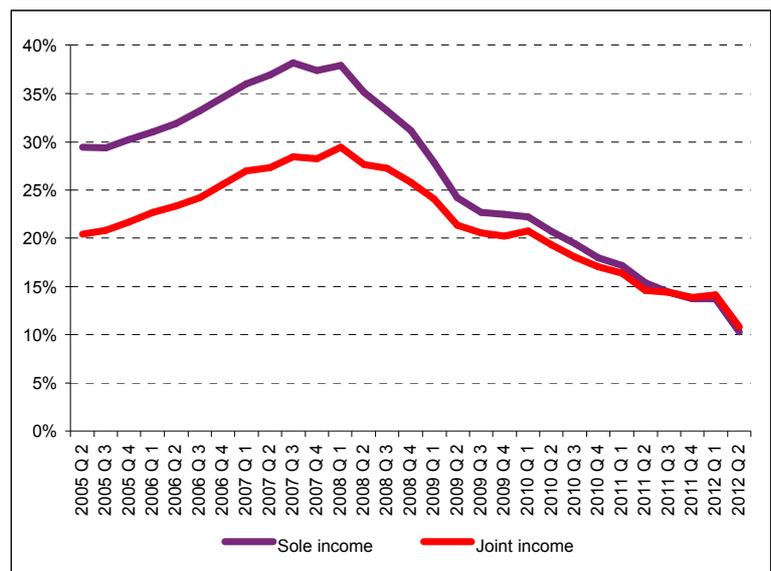
Exhibit 9.4: Average gross annual incomes of borrowers who took out mortgages in 2011



Source: FSA PSD

- Before the market downturn, borrowers on sole incomes were more likely to obtain interest-only mortgages than borrowers on joint incomes. This enabled them to increase the amount they could borrow and/or to reduce monthly payments at the same time.

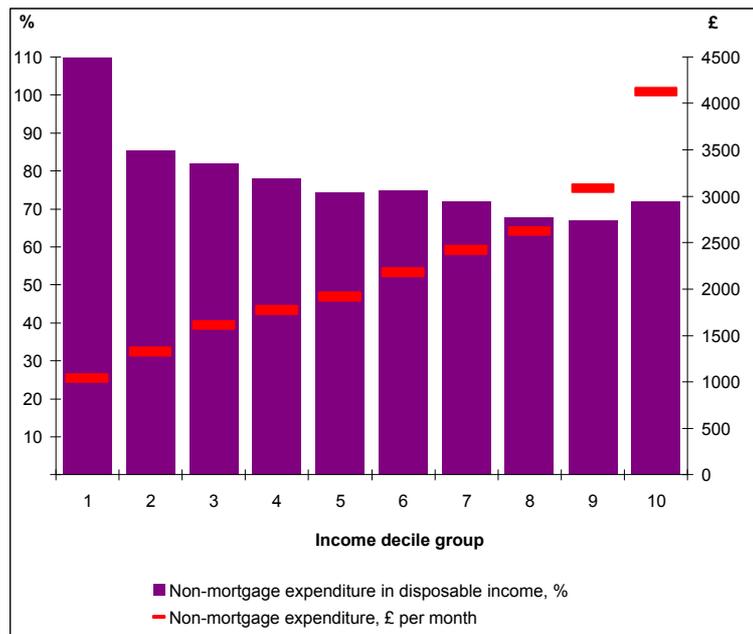
Exhibit 9.5: Proportion of interest-only mortgage sales, by type of borrowers' income



Source: FSA PSD

- We do not collect data on expenditure of mortgage borrowers, so we used an external source – the Living Cost and Food Survey (LCF)/ Expenditure and Food Survey (EFS). We looked at 13,000 households with a mortgage whose records are available in datasets from 2005 to 2010.
- The median non-mortgage expenditure of households was nearly £2,100 per month, or 77% of their normal disposable income. On average, borrowers on the lowest income spent more of their disposable income on non-mortgage expenditure.

Exhibit 9.6: Median non-mortgage expenditure and median percent of non-mortgage expenditure in normal disposable income, by income groups (deciles), 2005 to 2010



Source: LCF/EFS 2005-2010 datasets, FSA calculation

- The median mortgage expenditure during the same period was 17% of normal disposable income. The lowest-income households spent the highest proportion of their income on mortgage payments (28%).
- This suggests that there was a significant number of households with a mortgage whose normal income may not be enough to cover their expenditure and mortgage payments in full. Such households would have to use credit or savings to supplement their incomes.¹²

Exhibit 9.7: Median mortgage expenditure and median percent of mortgage expenditure in normal disposable income, by income deciles, 2005 to 2010

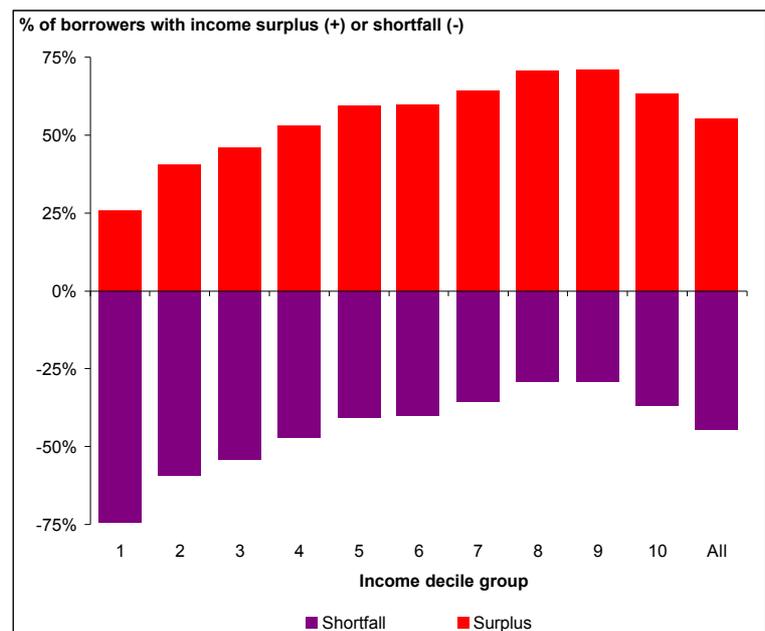


Source : LCF/EFS 2005-2010 datasets, FSA calculation

¹² See Chapter 7 this data pack for more information on unsecured debts of mortgage borrowers.

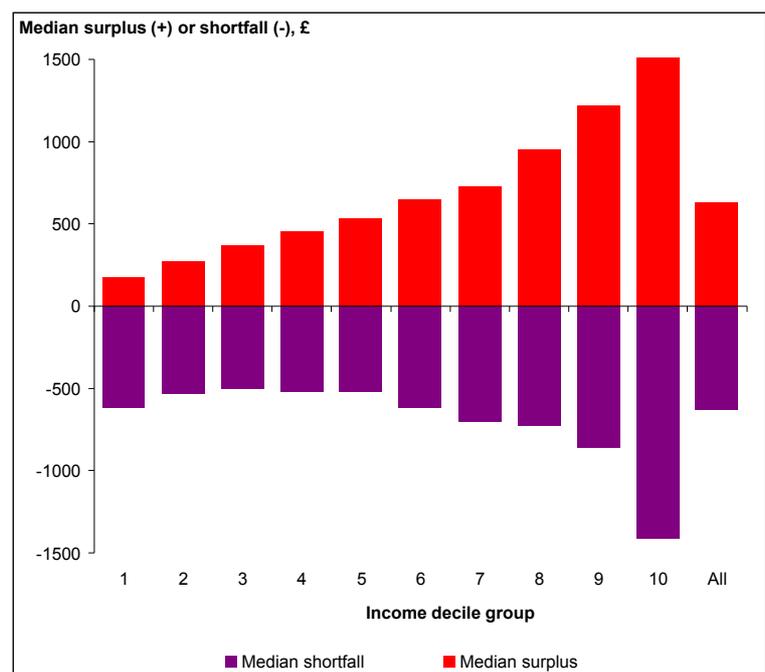
- We then worked out how much money mortgage borrowers had left after living expenditure and mortgage payments, by subtracting mortgage payments and non-mortgage expenditure from households' normal disposable income.
- Our calculation showed that 45% of households had no money left or had a shortfall that would have to be covered from savings or credit.
- The proportion of borrowers with a shortfall varied by income group. While the lower-income borrowers were affected the most, even within the higher-income groups a significant minority of households had a shortfall.
- The median shortfall and the median surplus were around £600 per month.

Exhibit 9.8: Proportion of households with income surplus or shortfall after living expenditure and mortgage payments, by income deciles group, 2005 to 2010



Source: LCF/EFS 2005-2010 datasets, FSA calculations

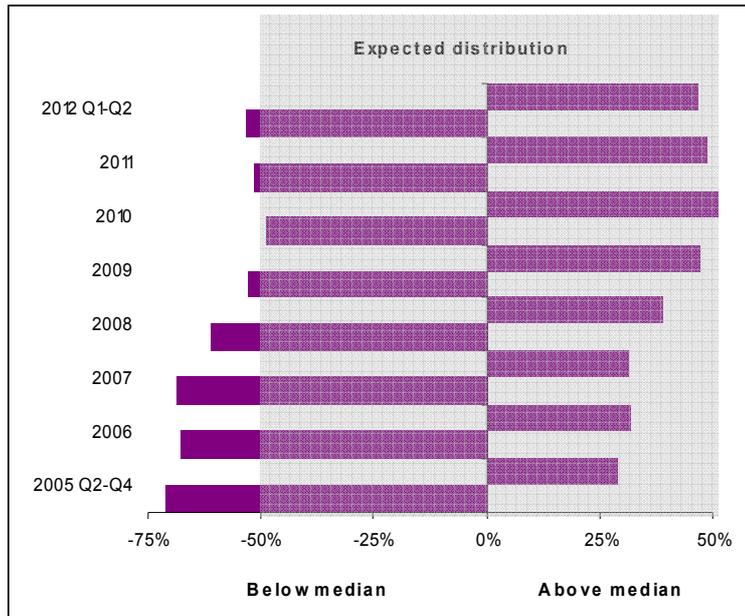
Exhibit 9.9: Median income shortfall or surplus, £ per month



Source: LCF/EFS 2005-2010 datasets, FSA calculation

- To get an indication of the extent of mortgages taken out in recent years that were foreseeably unaffordable, we compared the distribution of money available for non-mortgage expenditure from our Product Sales Data with the distribution of actual expenditure implied by the LCF/EFS data¹³.
- They were not consistent for 2005 to 2007. On average, the money available was less than the money spent, with more borrowers having less money available than the LCF/EFS data might imply they wanted to spend.
- This difference reduced in 2008 and largely disappeared from 2009 as lending criteria tightened.

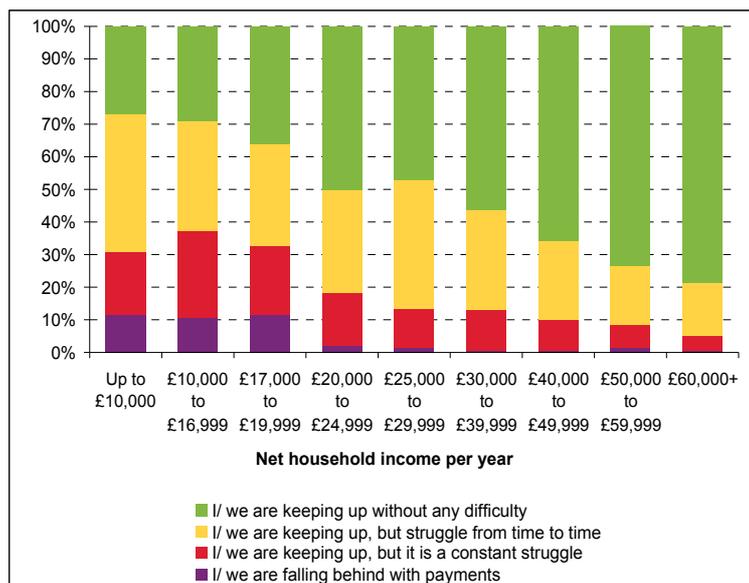
Exhibit 9.10: Money left for non-mortgage expenditure – expected and actual distribution



Source: FSA PSD, LCF/EFS 2005-2010 dataset for median expenditure, FSA estimate

- Data from independent surveys tells a similar story. As Exhibit 3.7 shows, a significant proportion of mortgage borrowers – on average, 47% according to BoE/NMG survey, 42% according to the YouGov for Shelter survey and 69% according to the Policis survey, struggle paying their bills and financial commitments at least from time to time, with 16%, 14% and 22% respectively constantly struggling.
- Lower-income households struggle the most. However, mortgage payment problems are not limited to those on low incomes.

Exhibit 9.11: How difficult is it for you to pay for your mortgage? – By income group

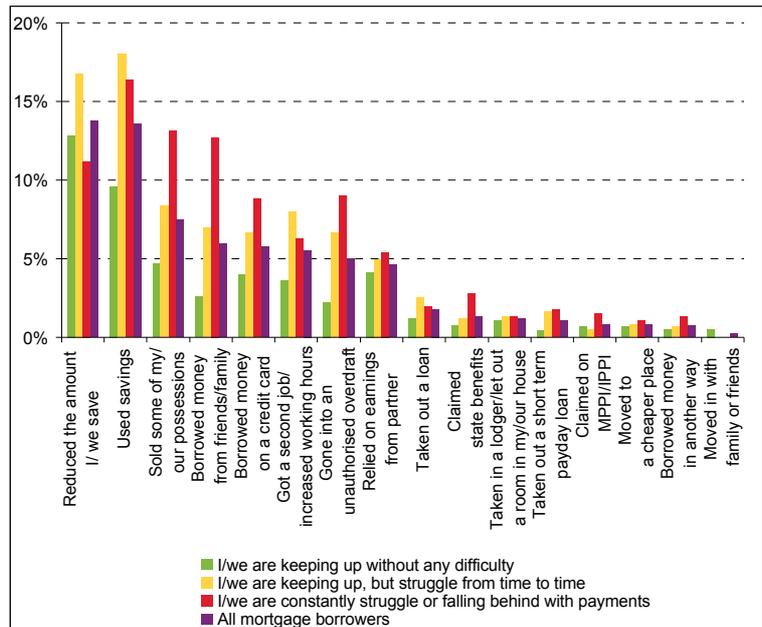


Source: YouGov online survey for Shelter (GB representative, 4,014 respondents, December 2011), FSA analysis

¹³ See Annex 1 that explains the methodology of this calculation

- The 2011 YouGov survey for Shelter shows that, even with the current low mortgage interest rates, many households have to supplement their income from other sources to afford mortgage payments.
- Borrowers who say that they constantly struggle with mortgage payments rely in particular on borrowed money. For example, 13% had to borrow from family and friends; 9% borrowed on credit cards; 2% took out a loan; around 2% took out a payday loan; and 1.3% borrowed in another way.

Exhibit 9.12: Have you or your partner in the last 12 months done any of the following to help meet your mortgage payments?

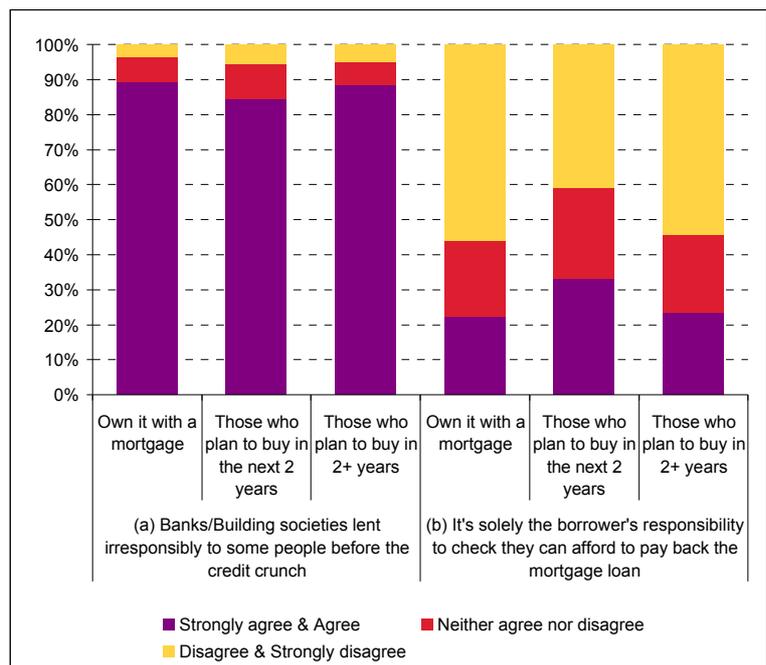


Source: YouGov online survey for Shelter (GB representative, 4,014 respondents, December 2011), FSA analysis

- According to the 2011 YouGov survey for Shelter, about 90% of mortgage borrowers and 85% of those who intend to buy a house in future thought that lenders lent irresponsibly to some people before the credit crunch.
- More than half of mortgage borrowers (56%) also said that it was not only the borrower's responsibility to check they could afford the mortgage loan.

Exhibit 9.13: What do people think? (Part 1)

- (a) Banks/building societies lent irresponsibly to some people before credit crunch;
- (b) It's solely the borrower's responsibility to check they can afford to pay back the mortgage loan



Source: YouGov online survey for Shelter (GB representative, 2,065 respondents, April 2011), FSA analysis

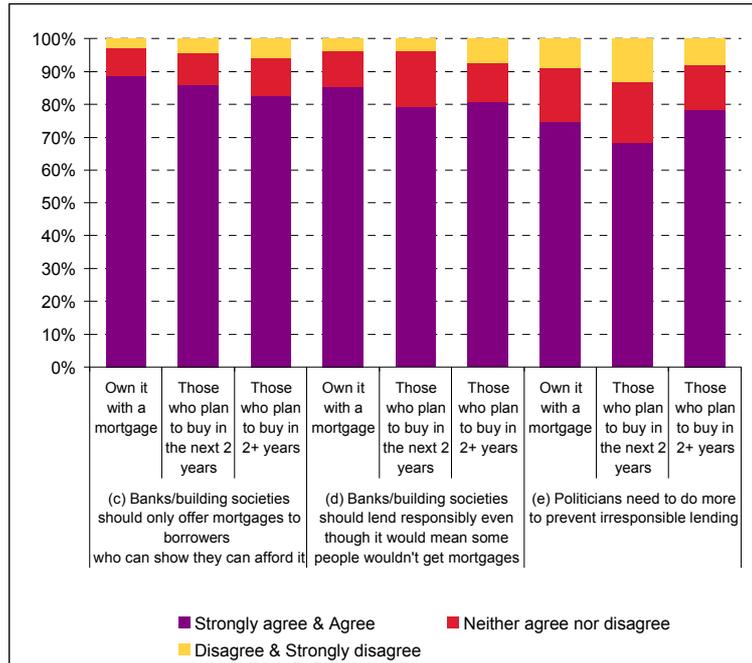
- Most respondents thought that lenders should lend responsibly and that borrowers should not be given mortgages that they could not afford, even if that meant that some people would not get mortgages. This included not only those who already own their houses, but also those who plan to buy in the future.
- Over 70% of respondents also thought that politicians needed to do more to prevent irresponsible lending.

Exhibit 9.14: What do people think? (Part 2)

(c) Bank/building societies should only offer mortgages to borrowers who can show they can afford it;

(d) Banks/building societies should lend responsibly even though it would mean some people wouldn't get mortgages;

(e) Politicians need to do more to prevent irresponsible lending



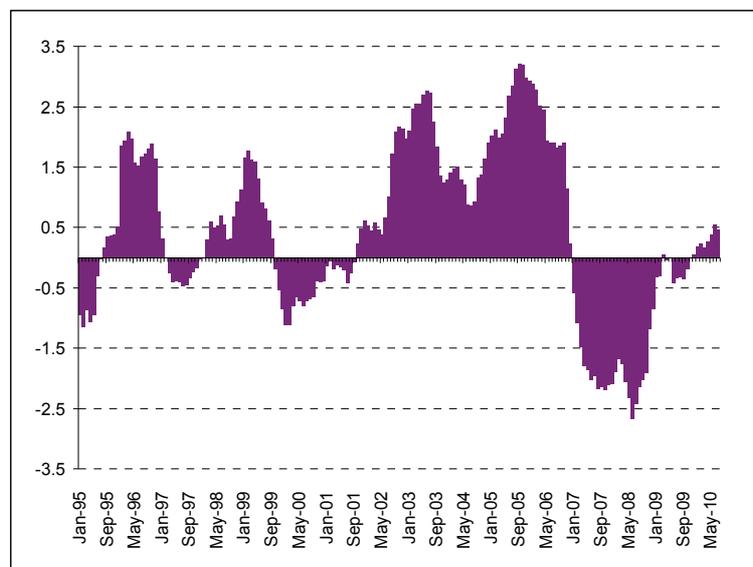
Source: YouGov online survey for Shelter (GB representative, 2,065 respondents, April 2011), FSA analysis

10

Mortgage interest rates

- Many mortgage borrowers experience an increase in interest rates after they take out their mortgage – e.g. 48% of mortgage borrowers who took part in the Policis survey said they had experienced a rate rise at some point.
- Obviously, this would impact most on borrowers on variable rates as their rate can increase shortly after their mortgage has started. However, borrowers on fixed rates may also see their interest rate increase when the initial fixed rate period ends.
- Borrowers who took out a two-year fixed rate mortgage in September 2005 could have seen their interest rate increasing by, on average, as much as 3.22 percentage points when they reverted to a standard variable rate (SVR) in September 2007.

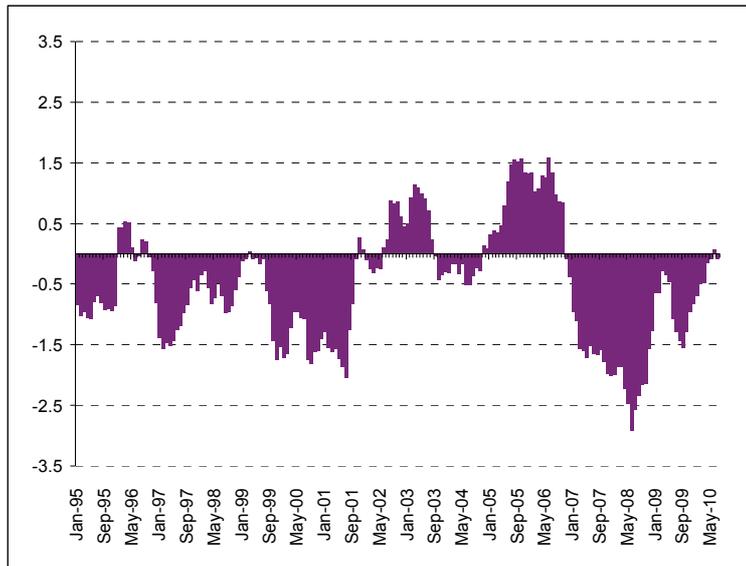
Exhibit 10.1: Estimated change in interest rate from a 2-year fixed rate to an SVR, by year of mortgage sale



Source: BoE, FSA calculation

- If they decided to remortgage instead at that point and take another two-year fixed deal, their interest rate could have increased, on average, by 1.53 percentage points.

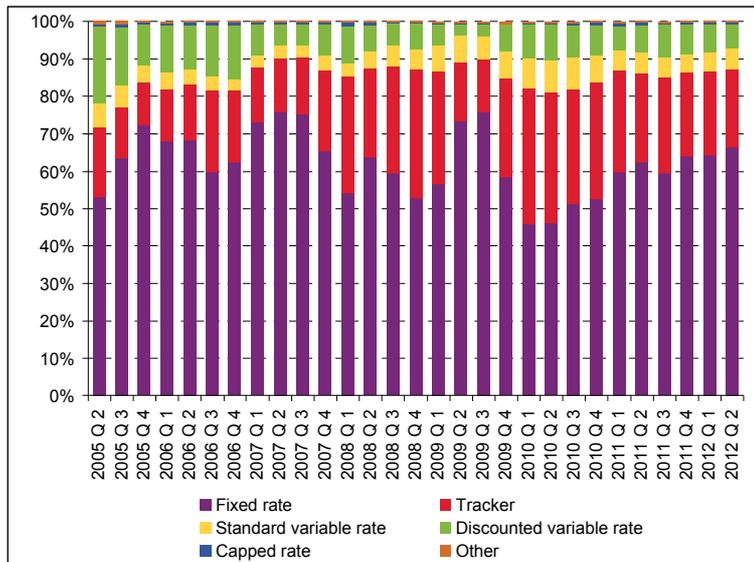
Exhibit 10.2: Estimated change from a 2-year fixed rate into another 2-year fixed rate, by year of mortgage sale



Source: BoE, FSA calculation

- Most new mortgages in the UK are fixed rate mortgages.

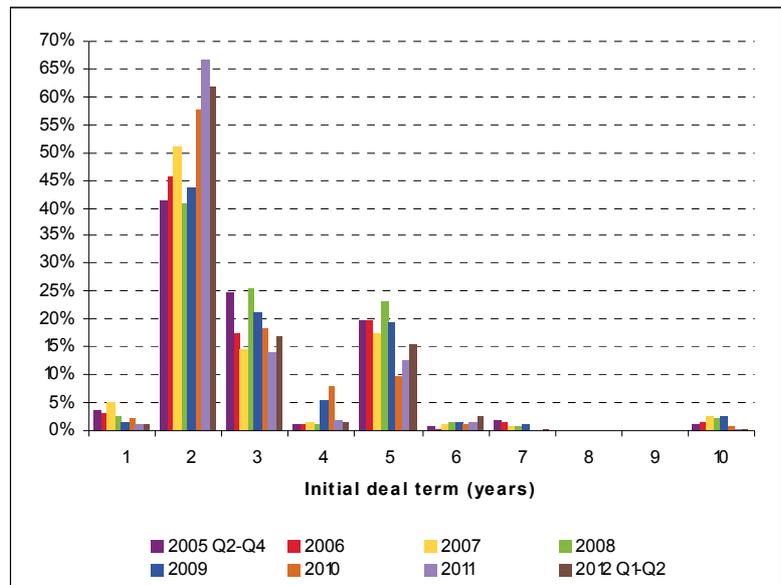
Exhibit 10.3: Structure of regulated mortgage sales, by type of interest rate



Source: FSA PSD

- However, it is still quite rare for mortgage borrowers to fix their rates for a long time. Most mortgages have interest rates fixed for just two years.
- The reasons are both in supply and demand: on one hand, lenders do not offer a large selection of longer-term fixed rate mortgages; on the other hand, borrowers tend to take short-term mortgages to prevent being locked into paying more than they need to over a long period when more competitive rates are available. Also, early repayment charges and typically higher interest rates probably discourage borrowers from taking longer-term fixed rate mortgages.

Exhibit 10.4: Distribution of initial term on fixed rate mortgages, by year of sale

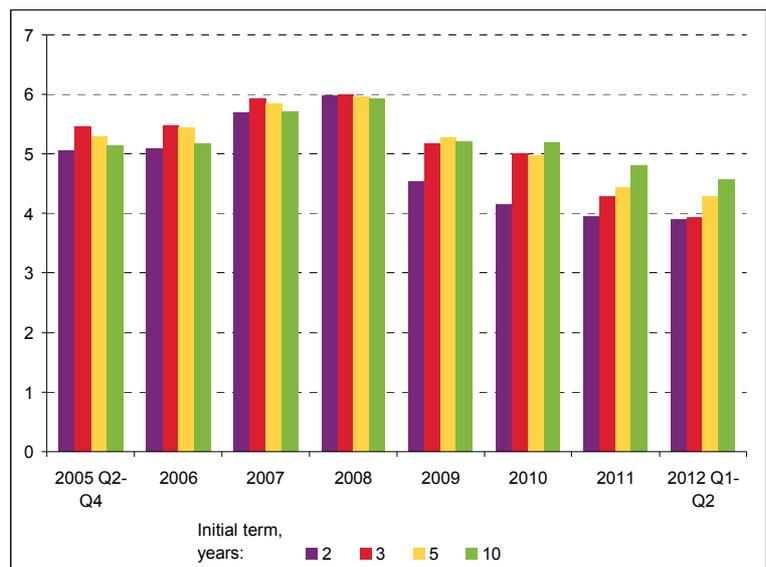


Note: In PSD, initial terms are optional for reporting, so our data may not represent the situation in the market fully

Source: FSA PSD

- The price differential between the longer- and the shorter-term fixed rate mortgages has become particularly apparent in recent years (2009-2012) because of the increased uncertainty about future interest rates.
- In 2010 and 2011, a ten-year fixed rate mortgage was, on average, around one percentage point more expensive than a two-year fixed rate mortgage. This is on the basis of headline rates only – there could be significant differences in arrangement and set-up fees, which we have not analysed.
- Recently, the proportion of shorter-term fixed rate mortgages has increased.
- In 2011, for example, 67% of all fixed rate mortgages were fixed for just two years. This could be due to the uncertainty about what might happen to interest rates in the future.

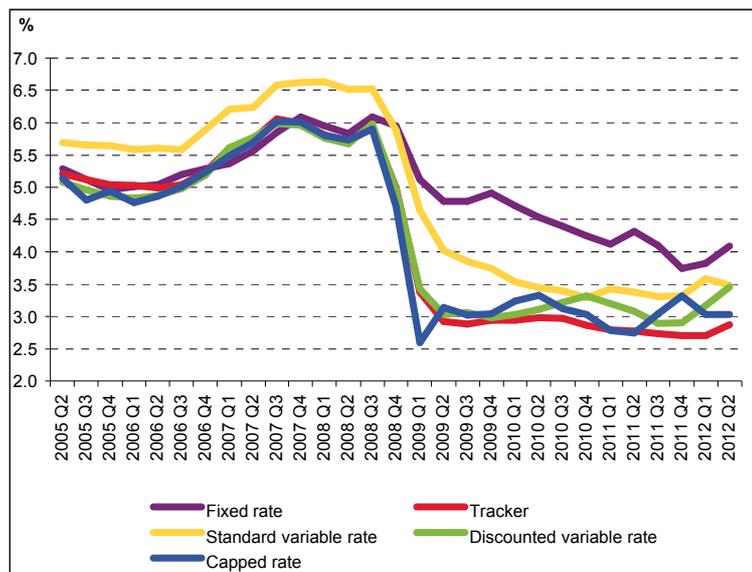
Exhibit 10.5: Average interest rate on fixed rate mortgages, by initial term



Source: FSA PSD

- Because of the uncertainty around future interest rates, from 2008, on average, fixed rate mortgages have become more expensive than variable rate mortgages.
- The take up of variable rate mortgages is, however, cyclical, and moves in line with the prevalent public opinion on the likelihood and imminence of rate rises. In 2010-2012, the take up of fixed rate mortgages increased on the expectation that the interest rates might increase relatively soon (see Exhibit 10.3).

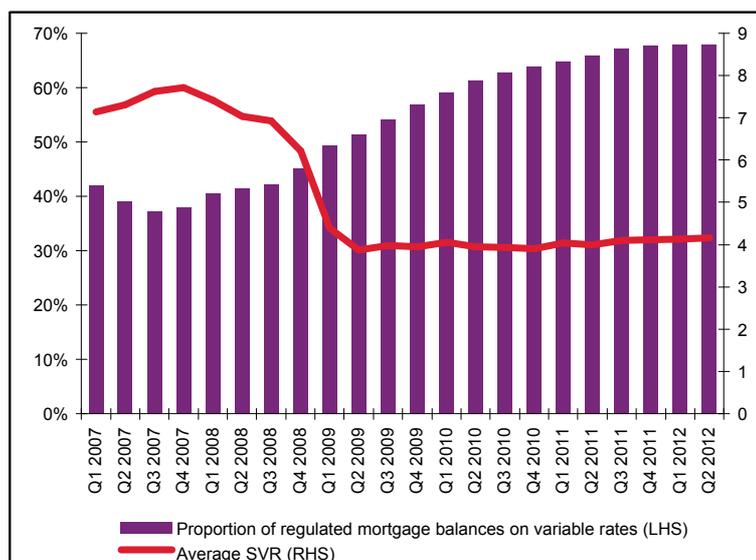
Exhibit 10.6: Average interest rate on mortgage sales, by type



Source: FSA PSD

- More importantly, however, following the recent significant reduction in SVRs, many borrowers whose fixed rate terms have ended have moved on to their lenders' SVRs and have not remortgaged.
- This has contributed to the very large increase in the proportion of variable rate mortgages on lenders' books.
- At the end of Q2 2012, 68% of regulated mortgage balances were on variable rates – compared with just 39% in Q2 2007.

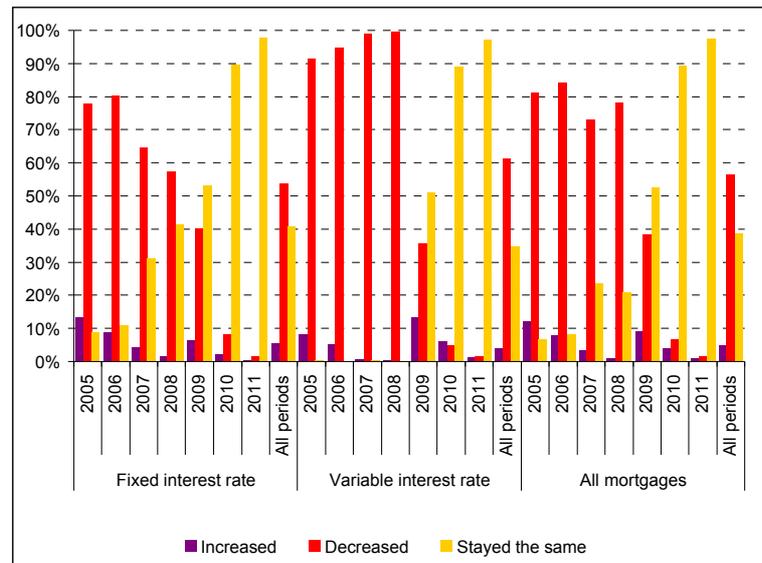
Exhibit 10.7: Change in the standard variable rate (SVR) and in the proportion of regulated mortgage balances on variable rates



Source: FSA MLAR, BoE

- From the data we have, we are unable to assess how many borrowers have experienced an increase in interest rates over the term of their mortgage and the impact this has had.
- We can, however, compare the interest rate borrowers had at the time when their mortgage was taken out with the current interest rate they paid in March 2012¹⁴.
- 56% of borrowers who have taken out a mortgage since April 2005 have seen their interest rates decrease and a further 39% have seen no change.
- Only a small proportion of borrowers (under 5%) had higher interest rates than initially.
- Almost all borrowers who took out variable rate mortgages in 2005-2008 are now benefiting from lower monthly payments.
- Borrowers with fixed rates who have fixed their mortgages for a shorter term (one to three years), and remortgaged for better rates or reverted to low SVRs have also benefited.
- However, a sizeable proportion of fixed rate borrowers with longer-term fixed periods, as well as borrowers who decided to fix their rates for another period after their initial term ended, have not seen a decrease in interest rate.
- Most borrowers whose interest rates have increased were initially on fixed mortgage rates. For example, of those borrowers who took out fixed rate mortgages in 2005, by March 2012, over 13% had a higher interest rate. This could have happened for two

Exhibit 10.8: Change in interest rates on mortgages, from year of sale to March 2012



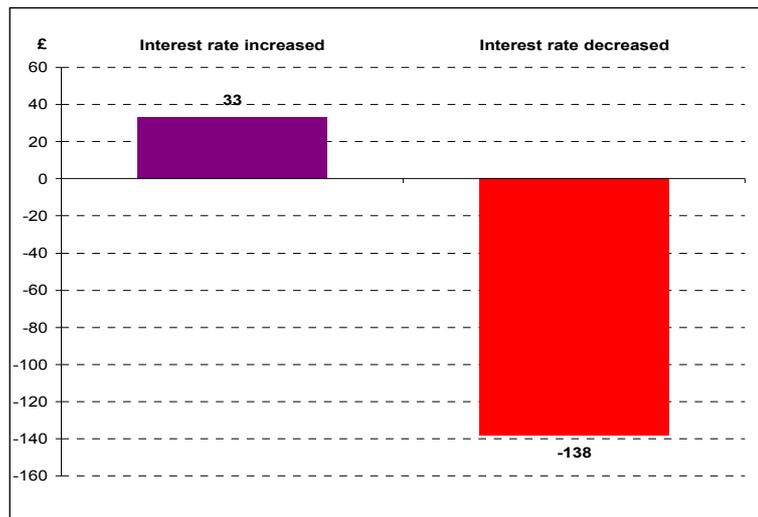
Source: PSD Performance data 2012

¹⁴ Note that the changes to SVRs introduced by lenders since March 2012 are not reflected in our data and not included in this analysis.

reasons: they could have taken out a new fixed rate mortgage, say in 2008, when the interest rates were generally higher than in 2005; or they could have reverted to their lender's SVR, which is higher than their initial rate, and they are unable or unwilling to remortgage to a better rate.

- For those borrowers who have experienced an increase in interest rates, on average, the increase is only £33 per month, so this is unlikely to have a major impact on the affordability of their mortgages.
- However, for those borrowers whose interest rates have decreased, the average monthly saving is £138.
- Almost 20% of mortgage borrowers are saving more than £200 per month on their mortgage payments.

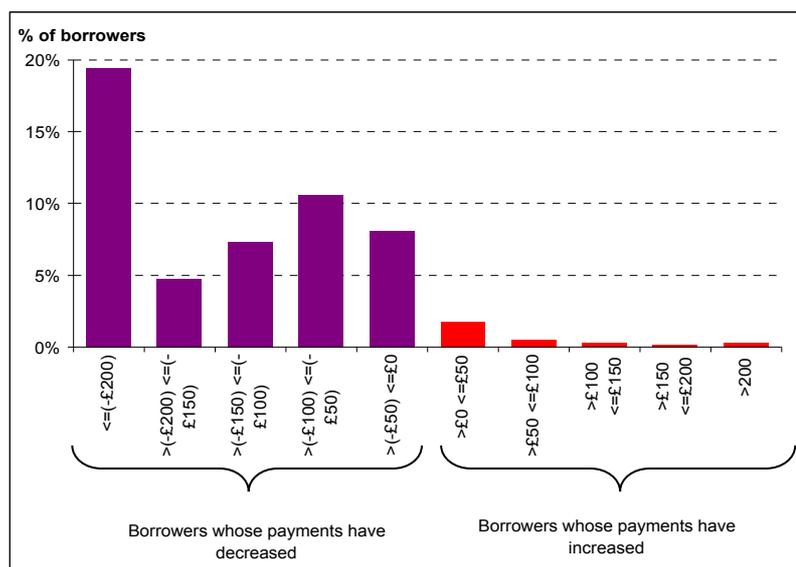
Exhibit 10.9: Median change in monthly mortgage payment



Note: The estimate is based on the sub-set of borrowers who made payments as planned, without overpayments or further borrowing that would have changed the size of their original mortgage.

Source: PSD Performance data 2012

Exhibit 10.10: Change in monthly mortgage payment

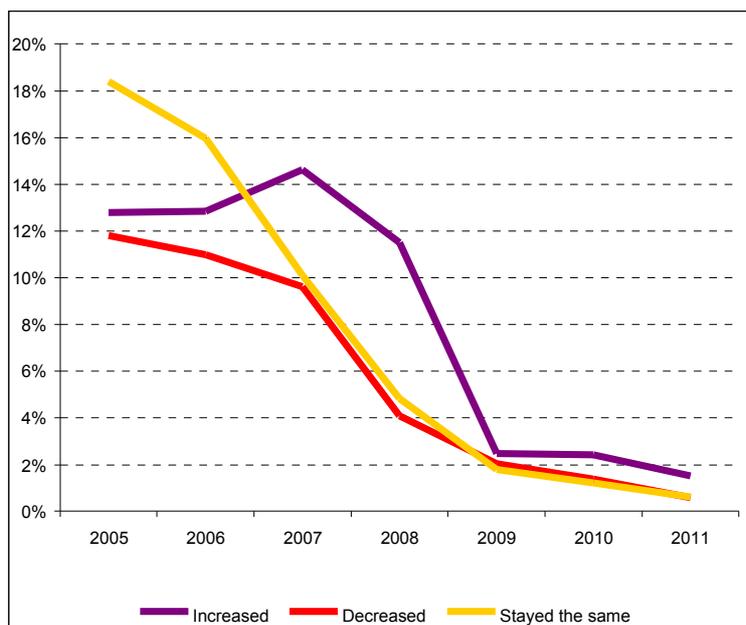


Note: Same as above (see Exhibit 10.9).

Source: PSD Performance data 2012

- The sizeable reduction in mortgage payments has clearly improved borrowers' ability to service their mortgages.
- For those borrowers who have experienced a decrease in interest rates, the proportion with current arrears or payment shortfalls is the lowest.
- As we have noted, a very small proportion of borrowers' interest rates have increased (just under 5%), and the average increase was quite small (£33 per month). However, even given this small increase, it follows from our data that these borrowers were generally more likely to have current arrears or payment shortfalls.

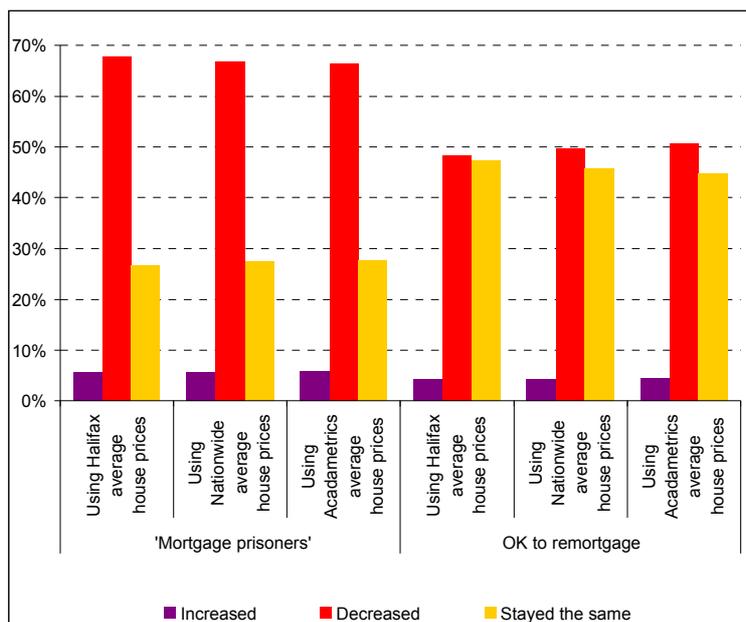
Exhibit 10.11: Borrowers with current arrears or payment shortfall, by type of interest rate change and year of mortgage sale



Source: PSD Performance data 2012

- As we explain in Chapter 5 of this data pack, up to 45% of current mortgage borrowers could be 'mortgage prisoners' – unable to remortgage or move house as they do not meet the more stringent lending criteria imposed by lenders since the market downturn.
- As at March 2012, nearly 70% of these borrowers were enjoying lower mortgage interest rates than their initial rates.
- A higher proportion of 'mortgage prisoners' than of those who can remortgage were benefiting from lower interest rates. This is because some of those who were able to remortgage (for example, for a fixed rate deal) could be on higher interest rates now than 'mortgage prisoners' who had to stay on their lenders' SVRs.

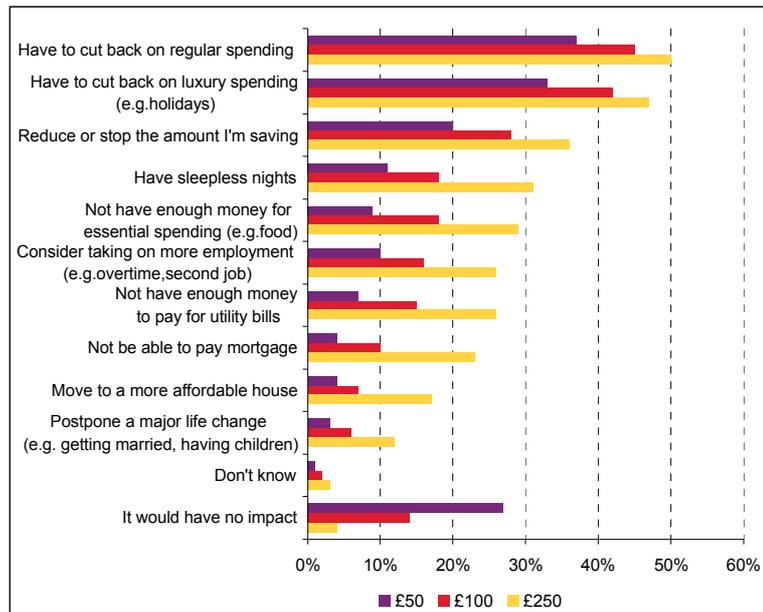
Exhibit 10.12: Mortgage interest rate at March 2012 compared with mortgage rate at origination



Source: PSD Performance data 2012

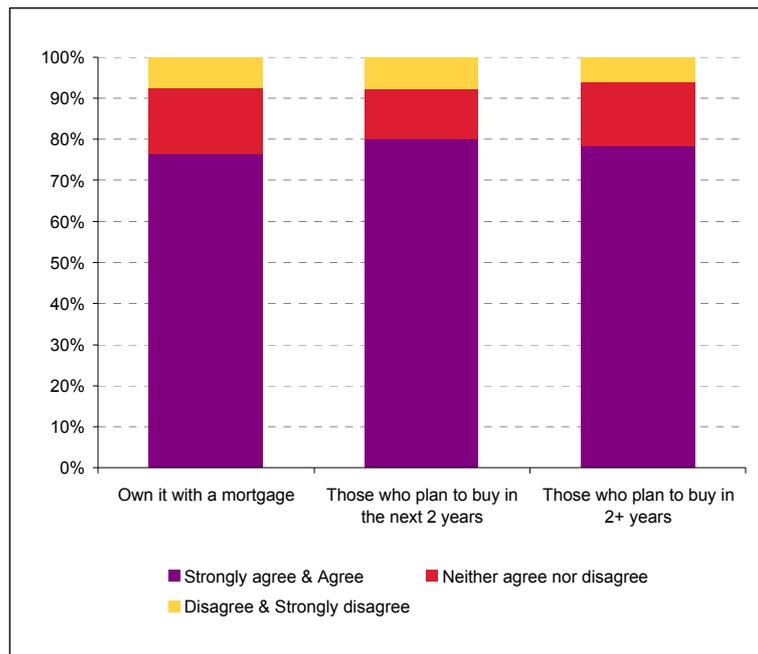
- According to a survey by Which?, many borrowers think that even a small increase in mortgage payments would cause significant financial distress (and this is at current low interest rates).
- For example, if mortgage payments increase by just £100 a month, 10% of people think they will not be able to pay their mortgage. A £250 increase would put over a quarter of all mortgage borrowers in this situation.
- To put these figures in context, on a £200,000 interest-only mortgage, a £100 increase is equivalent to an increase in the interest rate of 0.6 percentage points (e.g. from 3% to 3.6%) and a £250 increase is equivalent to an increase in the interest rate by 1.5 percentage points (e.g. from 3% to 4.5%).
- According to the 2011 YouGov survey for Shelter, the majority of those surveyed believed that lenders should check that borrowers are able to manage their mortgage payments when interest rates go up.

Exhibit 10.13: The impact of a monthly increase in mortgage repayments, March 2011



Source: Which?

Exhibit 10.14: Banks/building societies should check if the borrower will be able to manage their mortgage payments when interest rates go up



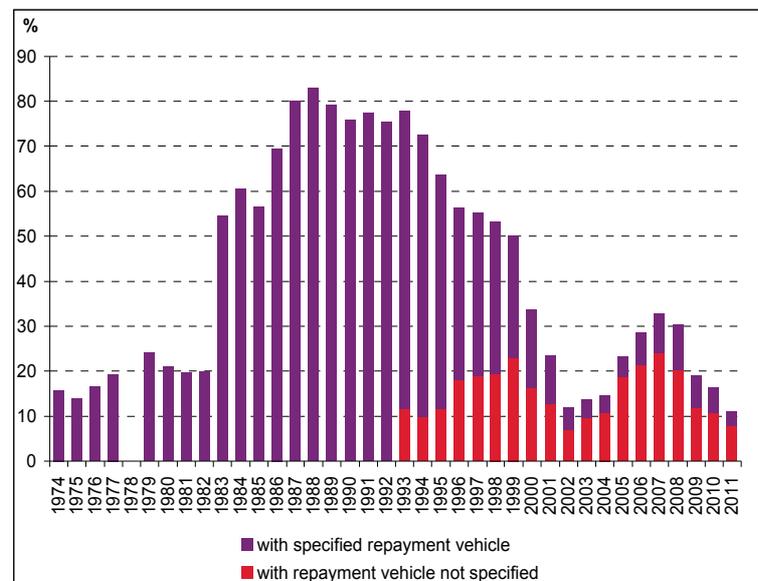
Source: YouGov online survey for Shelter (GB representative, 2,065 respondents, April 2011), FSA analysis

11

Interest-only mortgages

- Interest-only mortgages were originally a very small part of the mortgage market. Their use in the mass market had roots in the late 1980s when interest-only mortgages became attractive due to the tax regime and investment returns on endowment policies.
- Over time and through competitive pressure, lenders gradually relaxed their requirements for interest-only mortgages. They accepted a wider variety of repayment strategies, with a less robust assessment at the point of application and stopped requiring assignment of policies.
- The sale of interest-only mortgages rose sharply from 2002 to 2007, peaking at a third of all mortgage sales in 2007.

Exhibit 11.1: Interest-only lending, % of all new loans for house purchase, by year

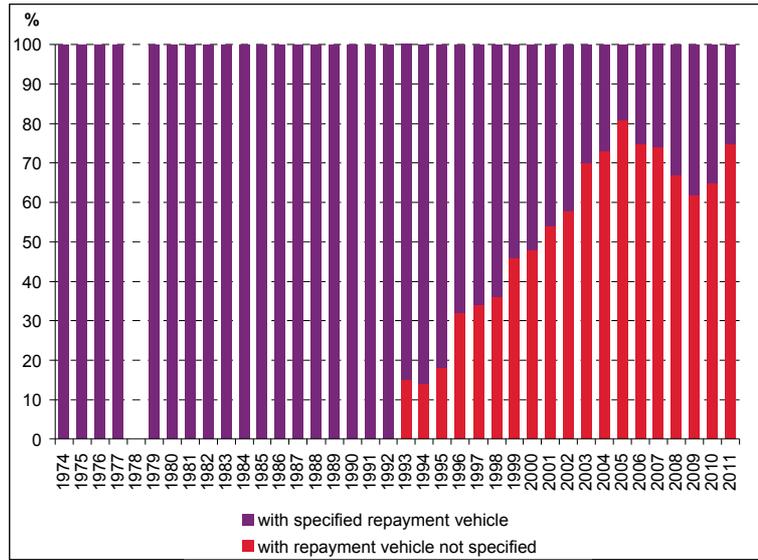


Note: Data for 1978 is not available.

Source: CML

- Many of these mortgages, around 75% in 2007, had no reported repayment strategy.

Exhibit 11.2: Repayment vehicles for interest-only mortgages, % in total interest-only sales for house purchase, by year

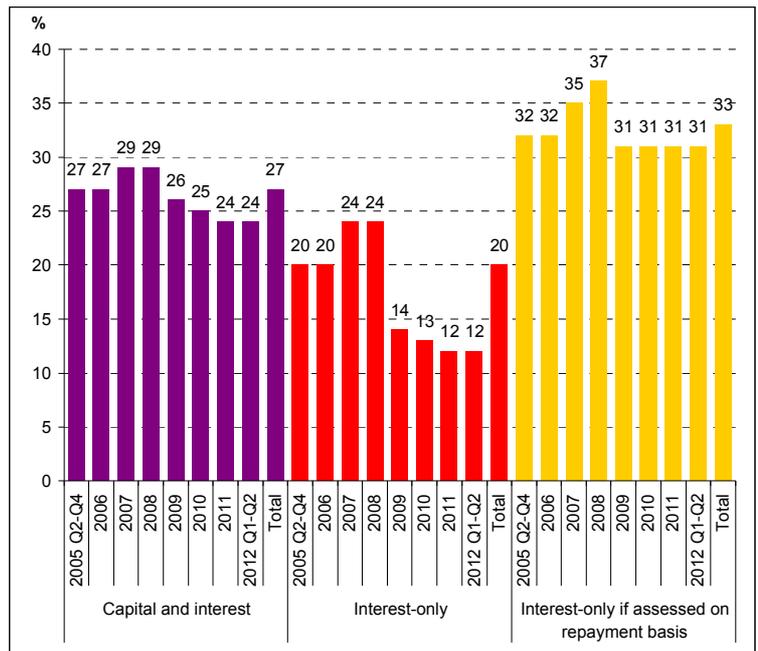


Note: Data for 1978 is not available.

Source: CML

- Consumers had an incentive to take interest-only mortgages because they could increase their borrowing capacity at a time of rapidly increasing house prices.
- Unsurprisingly, the average (median) monthly mortgage payments of interest-only borrowers take up a lower proportion of income than that of repayment borrowers.
- However, the same interest-only payments re-assessed on a capital and interest basis would take up a considerably higher proportion of income than for the average equivalent capital and interest mortgage.

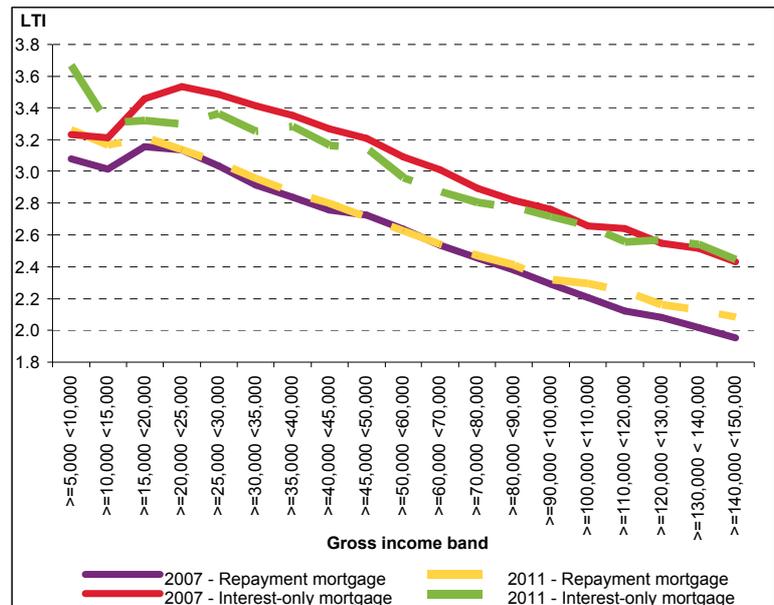
Exhibit 11.3: Median mortgage payment to net income ratio, by repayment method and year



Source: FSA PSD

- The easy availability of interest-only mortgages has allowed many consumers to take on larger mortgages than would be affordable on a capital and interest basis.
- Consumers have tended to take out larger mortgages on an interest-only basis than they do on a capital and interest basis, in terms of the size of mortgage in comparison to income.
- The trend has not changed significantly between 2007 (the peak of the market) and 2011.

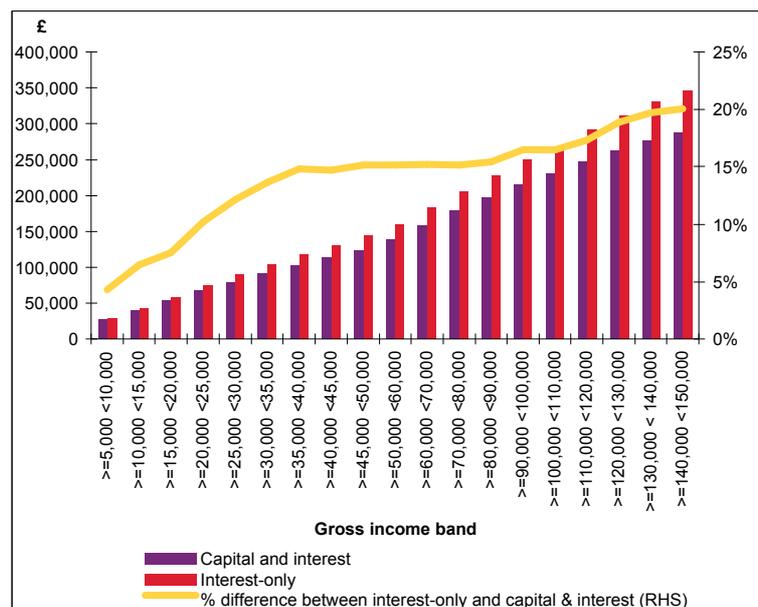
Exhibit 11.4: Median LTI on mortgages, by income group, 2007 and 2011



Source: FSA PSD

- This difference is observed in all income groups, both amongst the less well-off and better-off households.

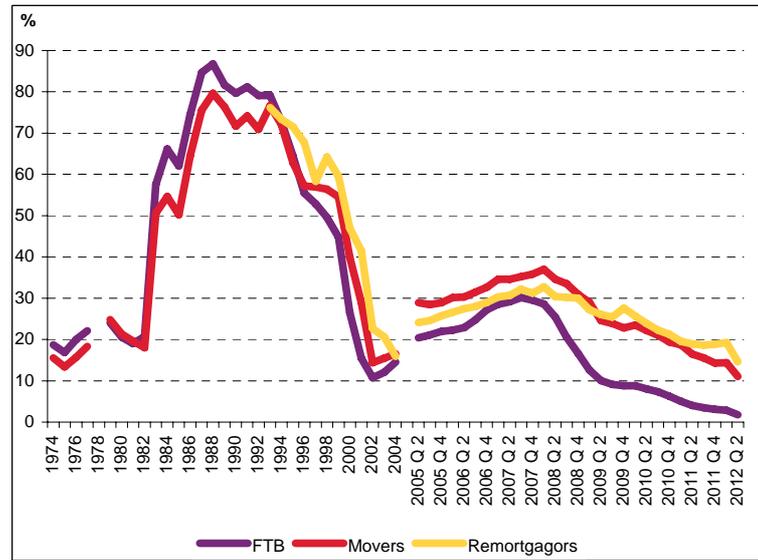
Exhibit 11.5: Average mortgage size, by income group (April 2005 - June 2012)



Source: FSA PSD

- Currently, FTBs are significantly less likely to have interest-only mortgages in comparison with those who remortgage or move house.
- In Q2 2012, only 2% of FTBs took out interest-only mortgages, compared with 11% of home movers and 15% of remortgagors.

Exhibit 11.6: Interest-only lending, % of all new loans, by year and type of borrower



Source: CML (1974-2004), FSA PSD (2005-2012)

- In the UK, around 41% of all loans secured on homes are currently on an interest-only basis, including 34% of regulated mortgage balances.
- On average, balances on interest-only mortgages are larger than on repayment mortgages as there are no regular repayments, and the size of interest-only mortgages does not decrease over time.

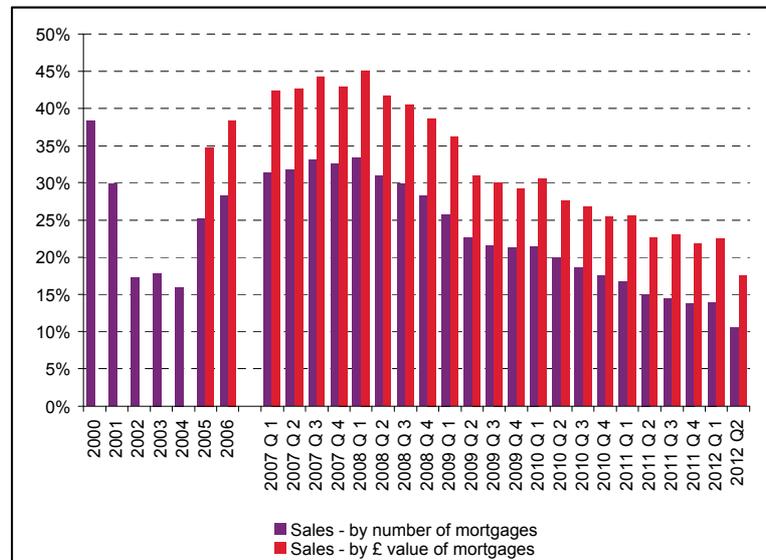
Exhibit 11.7: Interest-only: proportion in total number and value of outstanding regulated mortgages



Source: FSA MLAR

- Also, as already noted, borrowers often use interest-only mortgages in order to borrow more. Therefore the proportion of interest-only mortgages in total is significantly higher by value than by number of accounts.

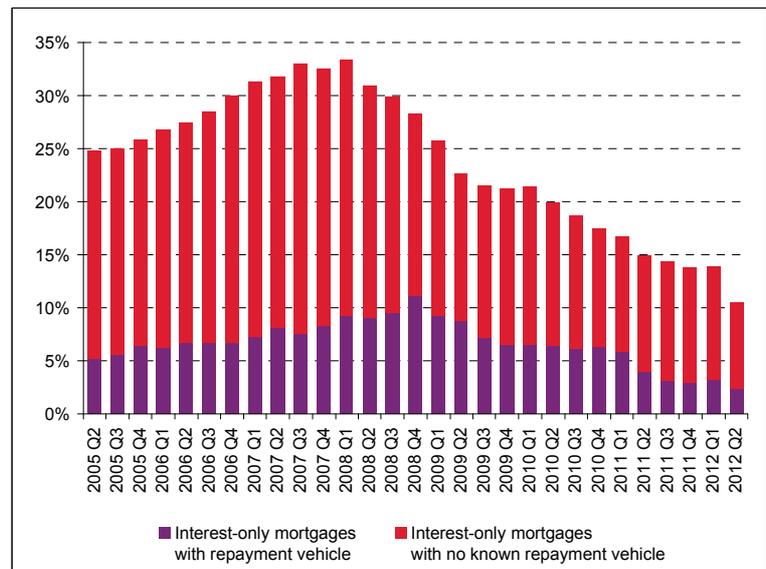
Exhibit 11.8: Interest-only: proportion in total number and value of sales



Source: CML (2000-2004 mortgage sales), FSA PSD (2005-2012 regulated mortgage sales)

- Although recently the sales of interest-only mortgages have been decreasing in relative terms, most still have no reported repayment strategy.

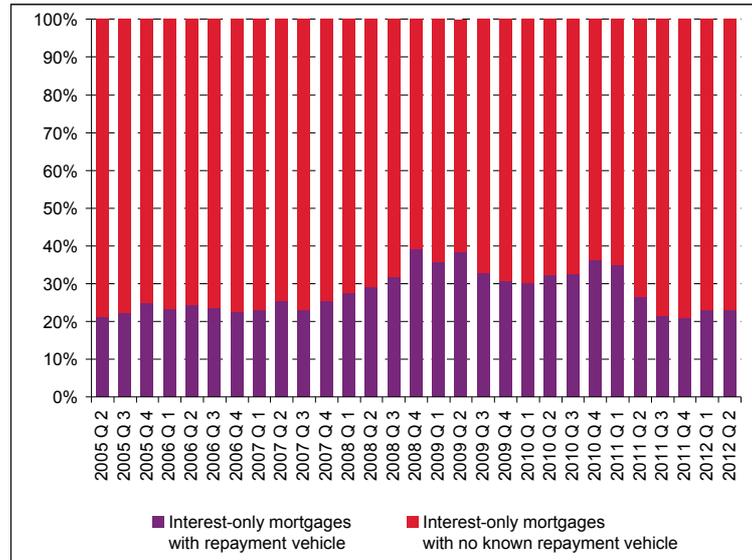
Exhibit 11.9: Proportion of interest-only mortgages in total regulated mortgage sales



Source: FSA PSD

- For example, in Q2 2012, 77% of all interest-only mortgages had no reported repayment strategy.

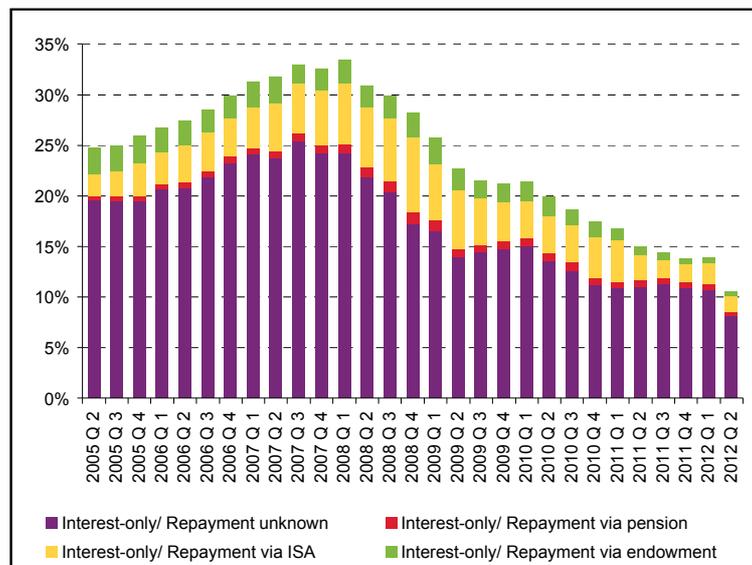
Exhibit 11.10: Interest-only mortgages with and without repayment vehicles



Source: FSA PSD

- Of those interest-only mortgages with a reported repayment strategy, ISAs and endowments are the most common.
- We do not know what proportion of borrowers continue contributing to these vehicles throughout the term of their mortgages and how these vehicles perform.

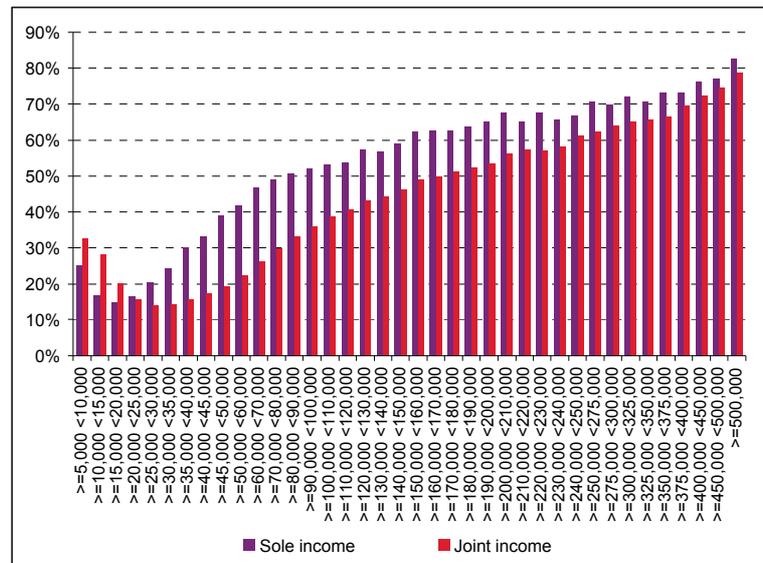
Exhibit 11.11: Interest-only mortgage sales by repayment method



Source: FSA PSD

- Borrowers with higher incomes are more likely to take out interest-only mortgages.

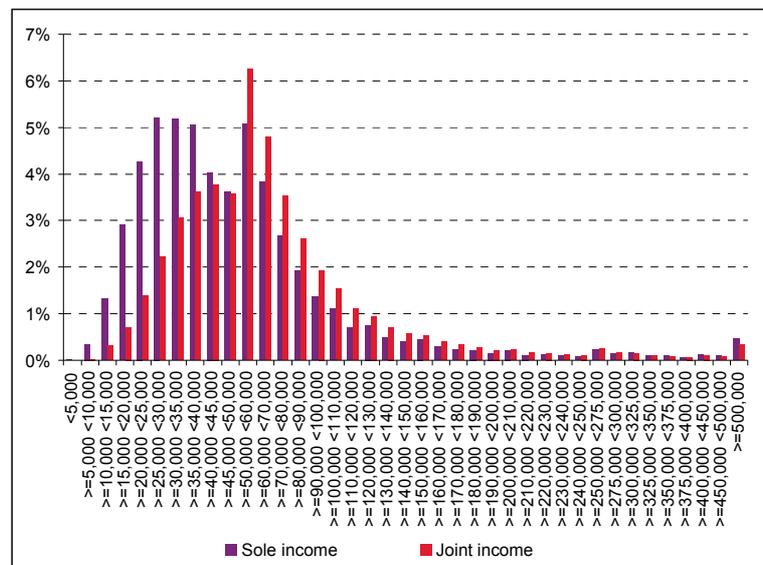
Exhibit 11.12: Interest-only mortgage sales, by income group and income type (April 2005 - June 2012)



Source: FSA PSD

- However, interest-only sales to borrowers that could be considered wealthier (for example, assuming a sole income of greater or equal to £100,000 or £200,000 for a joint income) are only 9% of all interest-only sales in the market.

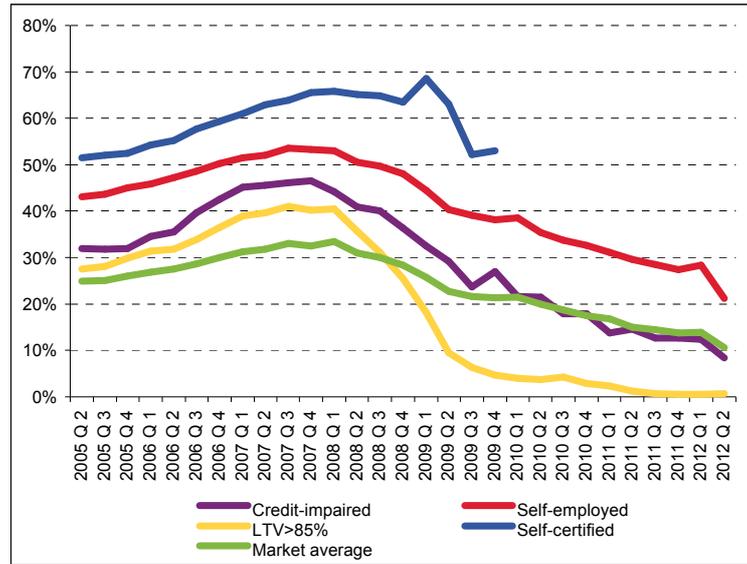
Exhibit 11.13: Proportion of income group in total interest-only sales (April 2005 - June 2012)



Source: FSA PSD

- Some types of borrowers are more likely than others to go for interest-only mortgages. This is most likely driven by affordability considerations.

Exhibit 11.14: Interest-only lending to some higher-risk borrowers



Source: FSA PSD

- Some of the riskiest mortgages on lenders' books are interest-only. Only around 43% of interest-only sales were lower-risk.

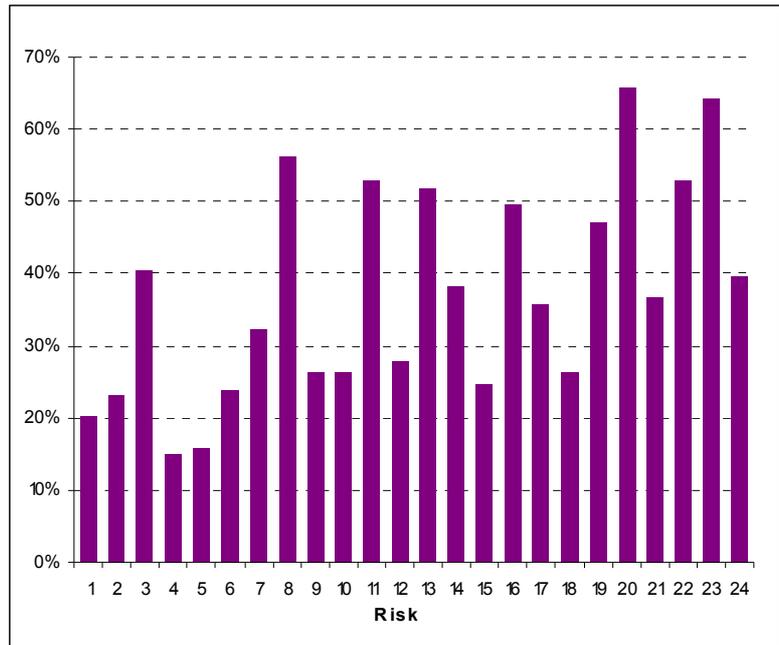
Exhibit 11.15: Risk combinations and interest-only lending

Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of interest-only in mortgage book, by risk type	% of risk type in total interest-only sales
1	NO	NO	NO	NO	NO	20%	43%
2	NO	YES	NO	NO	NO	23%	24%
3	NO	NO	YES	NO	NO	40%	14%
4	NO	NO	NO	YES	NO	15%	2%
5	NO	NO	NO	NO	YES	16%	0%
6	NO	YES	NO	YES	NO	24%	1%
7	NO	NO	YES	YES	NO	32%	1%
8	NO	YES	YES	NO	NO	56%	10%
9	NO	YES	NO	NO	YES	26%	0%
10	NO	NO	YES	NO	YES	26%	0%
11	NO	YES	YES	YES	NO	53%	0%
12	YES	NO	NO	NO	NO	28%	1%
13	NO	YES	YES	NO	YES	52%	0%
14	YES	YES	NO	NO	NO	38%	1%
15	YES	NO	NO	YES	NO	24%	0%
16	YES	NO	YES	NO	NO	50%	1%
17	YES	YES	NO	YES	NO	36%	0%
18	YES	NO	NO	NO	YES	26%	0%
19	YES	NO	YES	YES	NO	47%	0%
20	YES	YES	YES	NO	NO	66%	1%
21	YES	YES	NO	NO	YES	37%	0%
22	YES	YES	YES	NO	YES	53%	0%
23	YES	YES	YES	YES	NO	64%	0%
24	YES	NO	YES	NO	YES	39%	0%
Total						25%	100%

Source: PSD Performance data 2012

- A large proportion of the high-risk products in the market were sold on an interest-only basis.

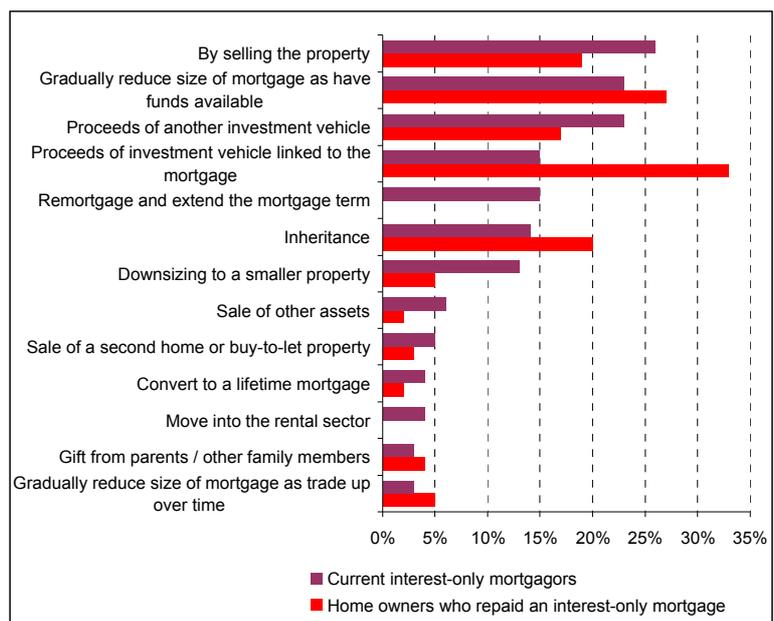
Exhibit 11.16: Outstanding mortgages: proportion of interest-only by risk type at origination



Source: PSD Performance data 2012

- Many borrowers with interest-only mortgages have less than certain plans for repaying the capital. They often rely on uncertain life events, such as the sale of the mortgaged property or inheritance.

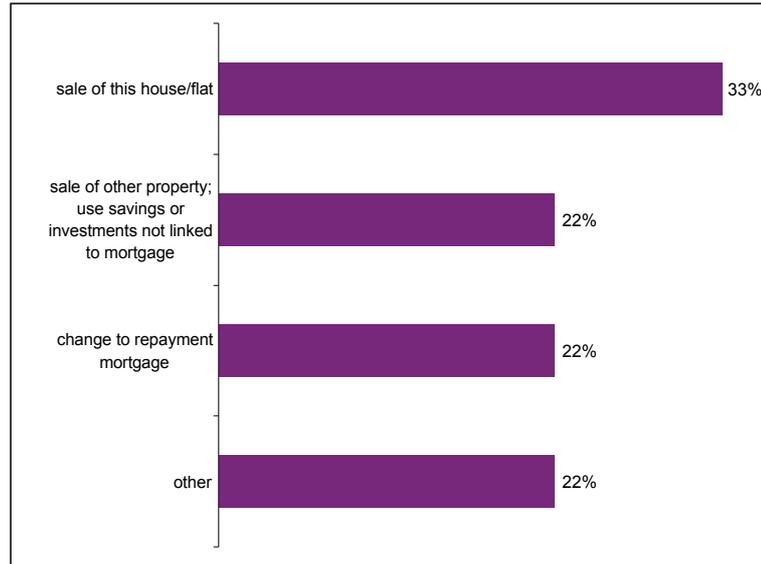
Exhibit 11.17: Intended plans and realised plans for interest-only mortgages



Source: Policis

- A significant proportion of borrowers plan to change to a capital and interest mortgage at some point in the future (22% according to the Survey of English Housing).

Exhibit 11.18: Owners with interest-only mortgage and no linked investment: how they propose to repay the mortgage (2010/11)

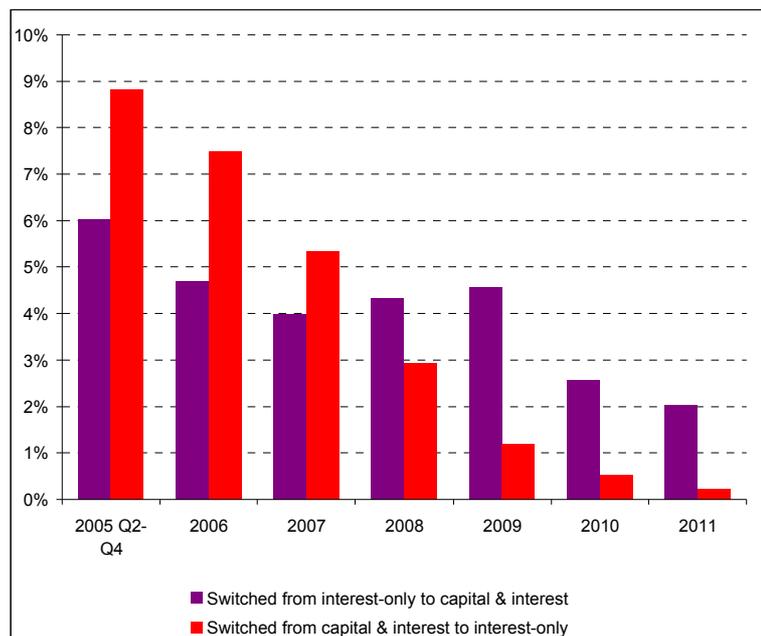


Note: 'Other' includes the following – 'take out investment with existing or new interest only mortgage', 'expected inheritance', 'other', 'don't know'

Source: DCLG

- Our data, covering only a relatively short period (seven years of mortgage sales) suggests that only a small proportion of interest-only borrowers change to a repayment mortgage.
- Of those who obtained interest-only mortgages in 2005, only 6% have switched to repayment mortgages.
- Over the same period, 8.8% of borrowers with repayment mortgages have switched to interest-only.

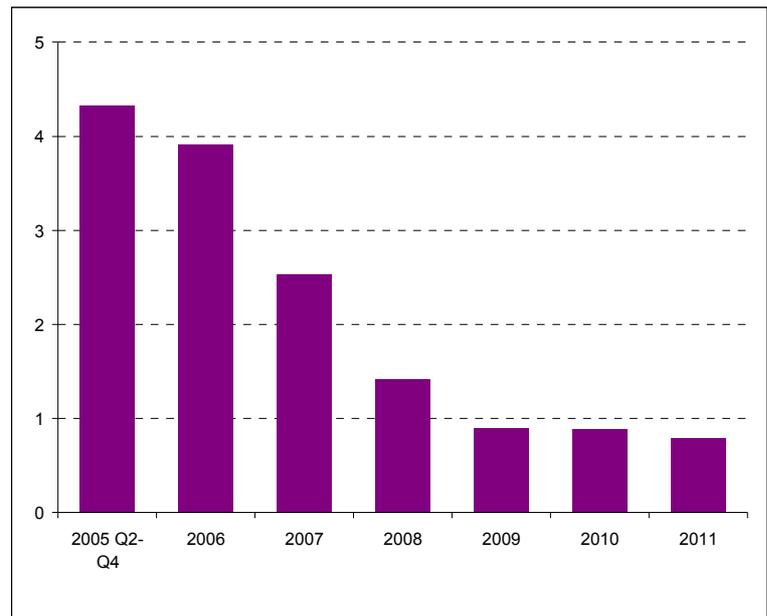
Exhibit 11.19: Borrowers who switched between interest-only and repayment mortgages by December 2010 - December 2011, by year of mortgage origination



Source: PSD Performance data 2012

- In absolute terms, amongst mortgages sold in 2005-2006, over four times as many switched from repayment to interest-only than from interest-only to repayment.
- As we noted in Chapter 6 of this data pack, interest-only mortgages are the most popular forbearance option that lenders offer to borrowers in difficulty.
- Although not captured in any of the regulatory returns, our analysis indicates that 30% of all forbearance cases included a switch to an interest-only mortgage.
- It is unknown what proportion of borrowers switch back to repayment mortgages when they get back on track and forbearance is no longer needed.

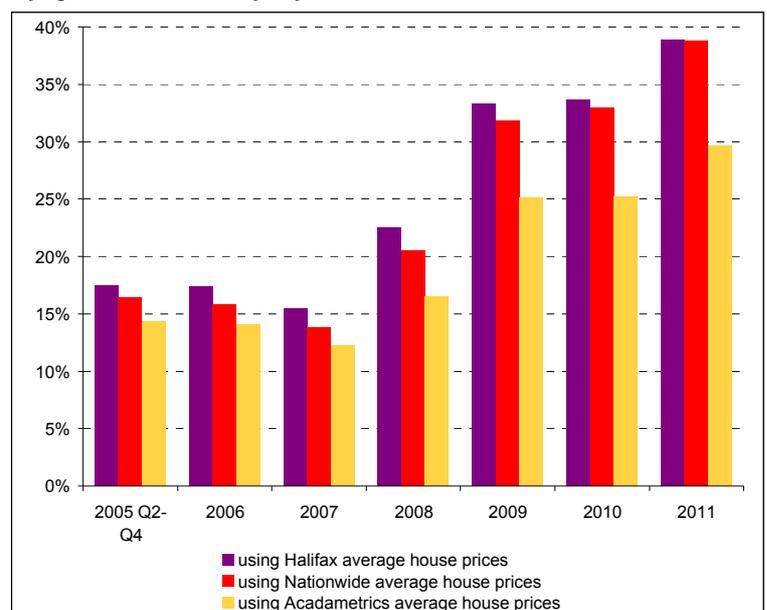
Exhibit 11.20: Ratio of switches: repayment to interest-only/ interest-only to repayment (by year of mortgage origination)



Source: PSD Performance data 2012

- Another popular capital repayment strategy is the sale of the mortgaged property.
- Around 26% in the Policis survey and 33% in DCLG's Survey of English Housing state 'sale of property' as their repayment plan.
- From the Policis survey, around 19% of borrowers have actually paid off their interest-only mortgage this way.
- From our data, we cannot tell exactly which borrowers plan to use downsizing as a repayment strategy for their interest-only mortgage. However, we can estimate which borrowers can realistically downsize, for example by comparing the amount of equity they have with the average house price in their region.
- We estimate that around 20% of borrowers who have taken out interest-only mortgages with no known repayment strategy in 2005-2011 may have sufficient equity to downsize to a smaller property.

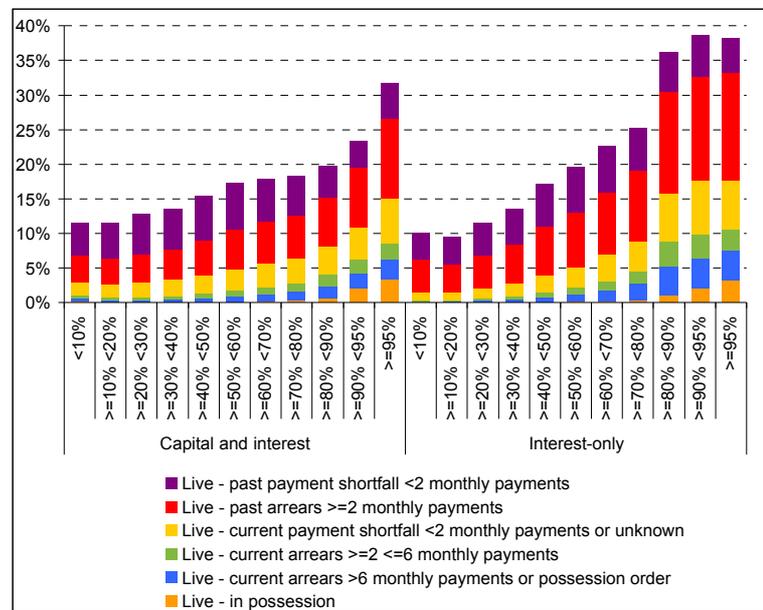
Exhibit 11.21: Interest-only sales to borrowers with no repayment vehicle: proportion who could downsize



Source: FSA PSD, Acadametrics, Halifax, Nationwide, FSA estimates

- Of those mortgages taken out in 2005-2007, around 15% could downsize. In 2009-2011, 35% could downsize. So there is a large difference depending on the year of mortgage origination. This is because lenders have considerably tightened their criteria around interest-only mortgages, with some now explicitly requiring that borrowers have a specified amount of equity in their homes if they want to use downsizing as a capital repayment strategy.
- Interest-only mortgages are more affordable in terms of their monthly payments as borrowers pay less towards their mortgage each month than they would pay for an equivalent repayment mortgage.
- The risks of interest-only lending for consumers typically crystallise when the capital element has to be repaid, many years after the mortgage has been taken out.
- Therefore, the risk of interest-only lending often does not translate into higher arrears rates. However, interest-only mortgages do perform worse than repayment mortgages at higher LTV bands, where it is more likely that the borrower opted for the interest-only mortgage for affordability reasons.

Exhibit 11.22: Performance of interest-only and repayment mortgages, by LTV band at origination

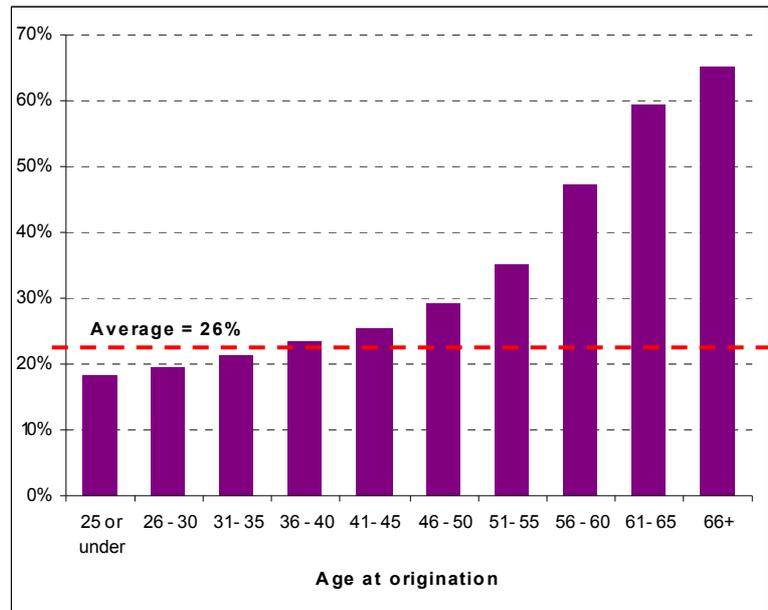


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

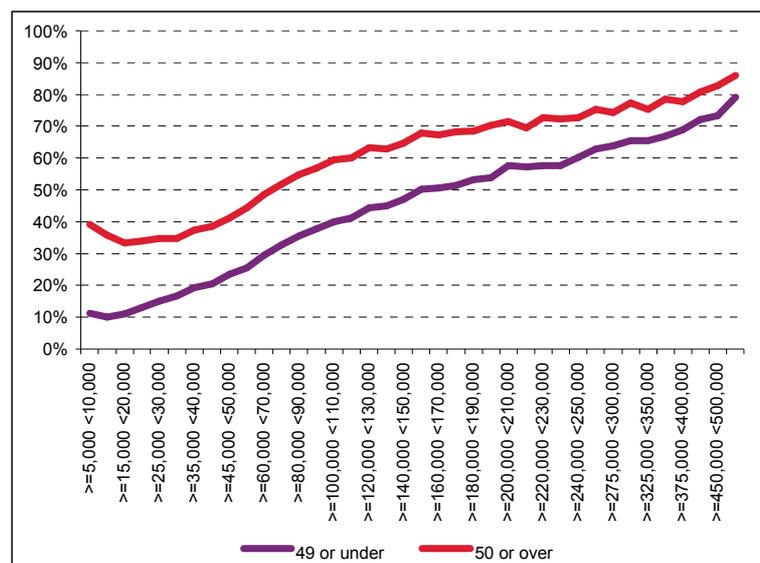
- Older borrowers are more likely to have an interest-only mortgage, regardless of their level of income.
- This is because most mortgages sold in the 1980s and early 1990s (and now approaching maturity) were interest-only, or because some borrowers with longer-standing mortgages switched to interest-only in order to increase their borrowing or to reduce repayments.

Exhibit 11.23: Proportion of interest-only mortgage sales, by borrower's age at origination (April 2005 – December 2011)



Source: PSD Performance data 2012

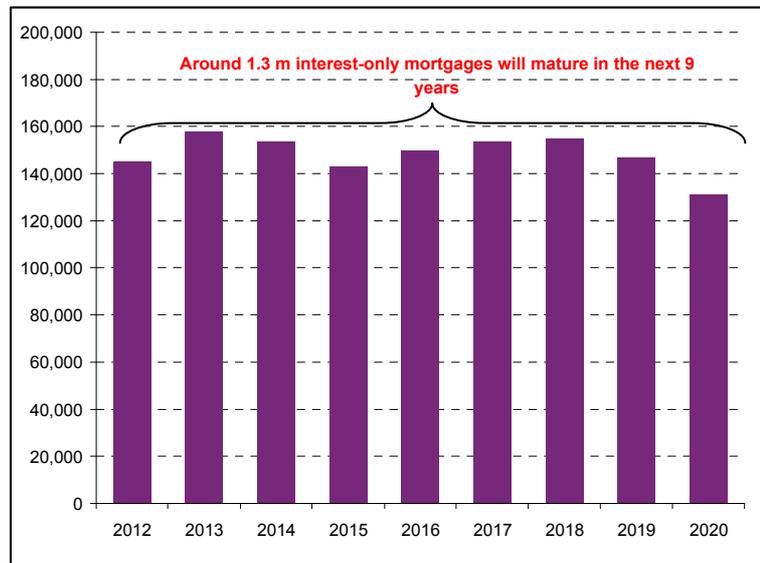
Exhibit 11.24: Proportion of interest-only sales, by age and income group (April 2005 – June 2012 sales)



Source: FSA PSD

- In the next nine years (2012-2020), 1.3m interest-only mortgages worth around £111bn will be due for repayment.
- The vast majority of these mortgages are owner-occupier mortgages.¹⁵ On average, around 150,000 interest-only mortgages will be due for repayment each year.

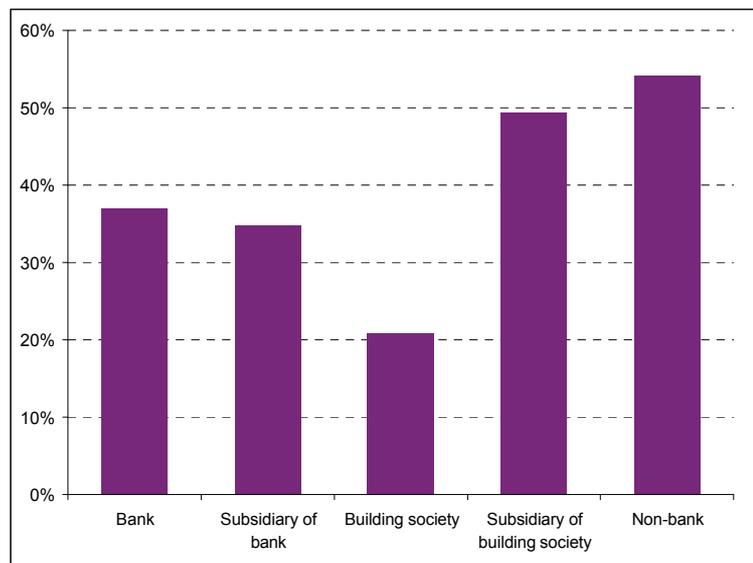
Exhibit 11.25: Number of interest-only mortgages maturing in the next nine years



Source: CML

- Overall, non-banks have the highest exposure to interest-only lending (54%) and building societies have the lowest (21%). However, the exposure of subsidiaries of building societies is comparable to that of non-banks and stands at 49%.

Exhibit 11.26: Regulated interest-only mortgage balances, by type of lender, Q2 2012



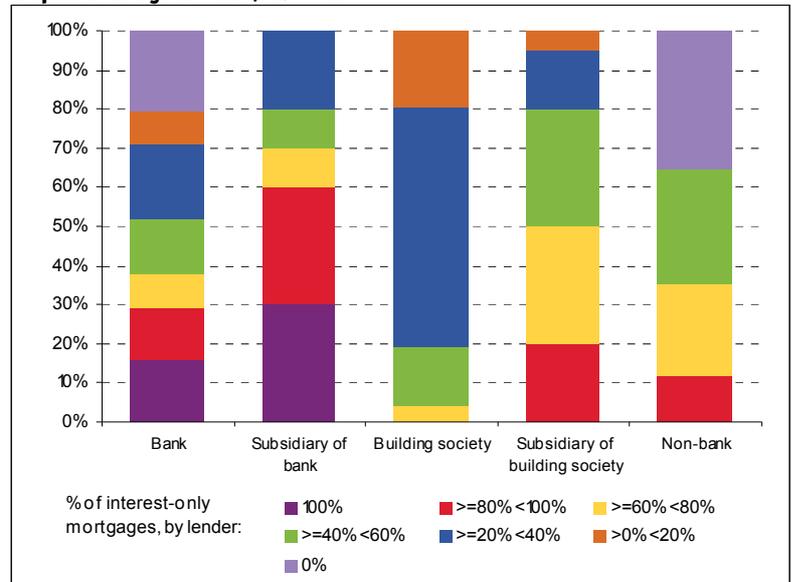
Note: Exhibits 11.26 and 11.27 exclude lenders whose business is mostly in niche markets, such as private banking, bridging finance and equity release.

Source: FSA MLAR

¹⁵ Most BTL mortgages were sold after 2000, thus assuming typical 25 year terms, they are not expected to mature in the next nine years

- The exposure to interest-only lending greatly varies depending on the lender - from 0% to 100%. For some lenders, over 60% of their lending book is interest-only.

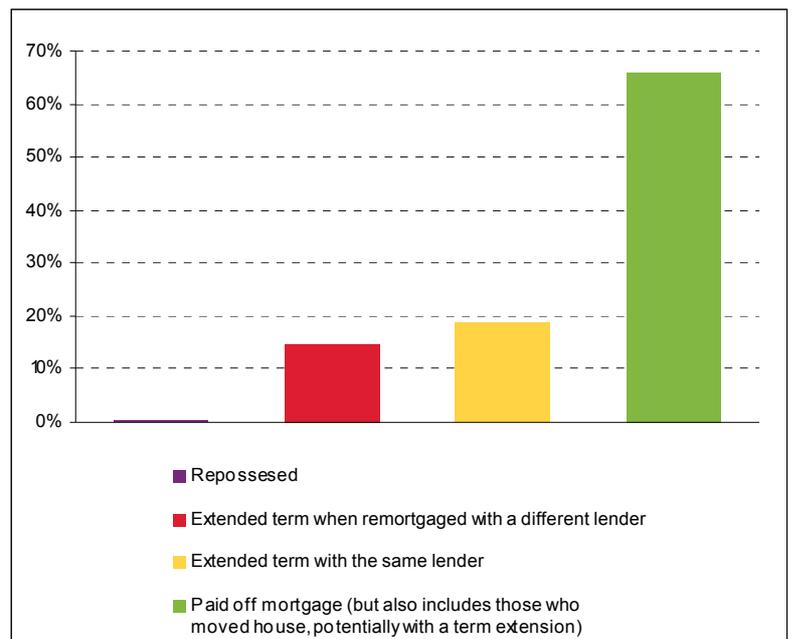
Exhibit 11.27: Regulated interest-only mortgage balances, % exposure by lender, Q2 2012



Source: FSA MLAR

- Evidence from the industry suggests that many interest-only mortgages could not be repaid in full when the term is up. Instead, lenders typically have to extend the repayment term.
- We have no information on the proportion of interest-only mortgages that are successfully repaid following term extensions.
- At present, we do not have comprehensive data on repayment of interest-only mortgages at maturity. To get an indication of whether such mortgages are repaid on time, we have analysed around 33,000 regulated mortgages with a term of five years that were taken out between April 2005 – September 2006.
- Of those, around 19,000 mortgages were interest-only. All of these mortgages were due to be paid off by the end of December 2011.
- As at March 2012, a significant proportion of these mortgages had not been paid off (at least 34%) and had their terms extended.¹⁶

Exhibit 11.28: Mortgages sold in April 2005 - September 2006 with a term of 5 years: where are they now, after their contractual term has ended?

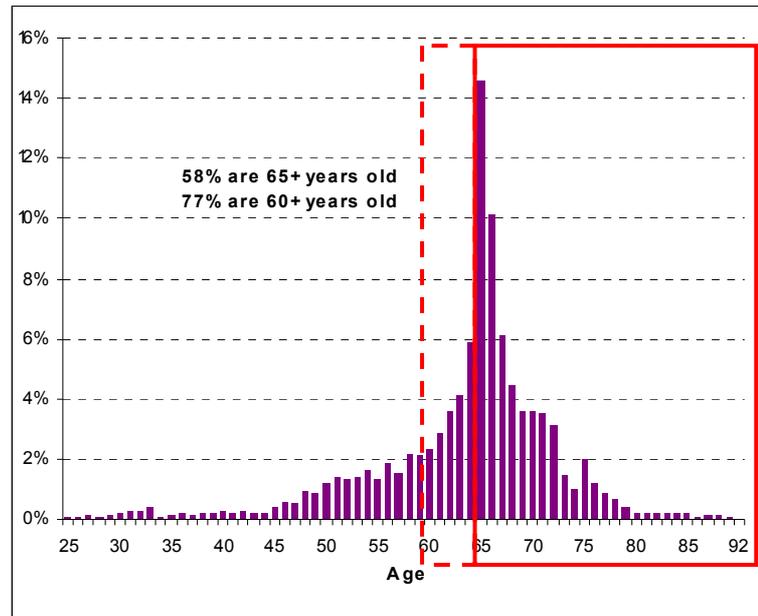


Source: PSD Performance data 2012

¹⁶ As we are unable to track outcomes for borrowers who moved house, the true proportion is probably higher.

- From this analysis, where the term had been extended, 58% of the borrowers were over 65; 77% were over 60 years old; the average balance was around £112,000; and 73% had no specified repayment strategy.

Exhibit 11.29: Age of interest-only borrowers who extended mortgage term beyond planned maturity



Note: Interest-only mortgages taken out in April 2005-September 2006 for 5 years

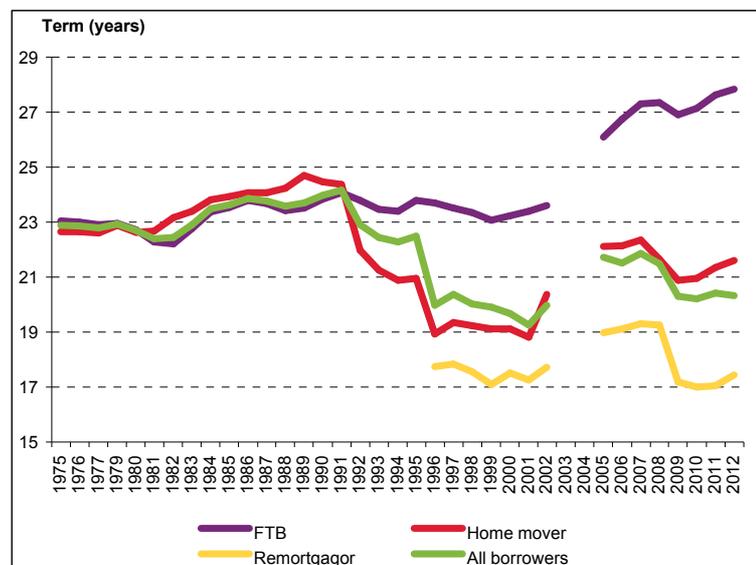
Source: PSD Performance data 2012

12

Mortgage terms

- The average mortgage term across the market currently stands at 20 years and has somewhat decreased since 2005 when we started to collect PSD (and also from its peak level in the late 1980s).
- Mortgage terms to first-time buyers (FTB) have been increasing over the past decade. The average FTB term in 2011 and Q1-Q2 2012 was 28 years.
- Over the same period, the average mortgage terms of other borrowers have decreased.

Exhibit 12.1: Average mortgage term at origination, by type of borrower

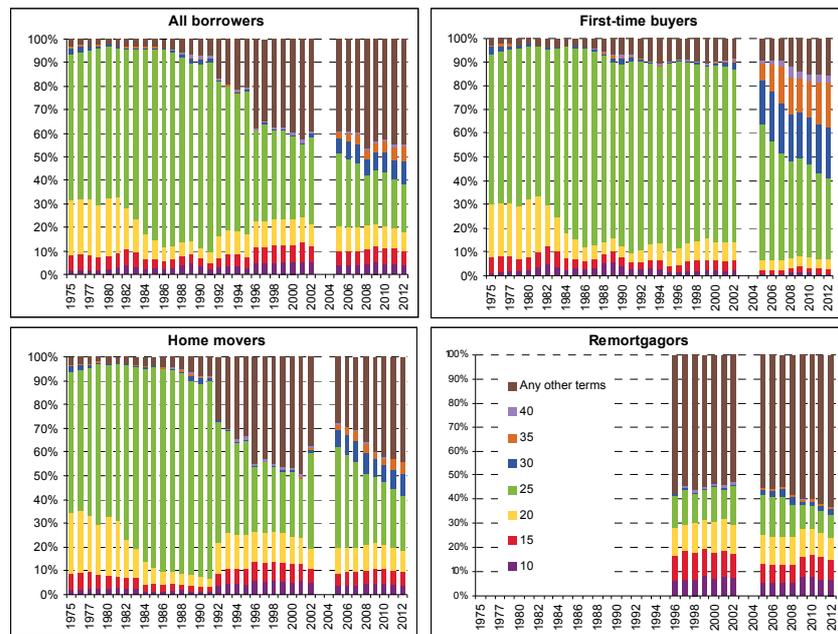


Note: Data on mortgage terms in 2003-2004 is not available.

Source: SBS, SML, FSA PSD

- By frequency of sales, 25-year term remains the most popular mortgage term in the market.
- Longer-term mortgages are less common and are mainly taken out by FTBs.
- A high level of non-standard terms (e.g. eight years, 22 years etc.) shown in the data for former owner-occupiers (home movers and remortgagors), is probably indicative of the fact that many borrowers remain on their original mortgage term when they remortgage or move house.

Exhibit 12.2: Popular mortgage terms

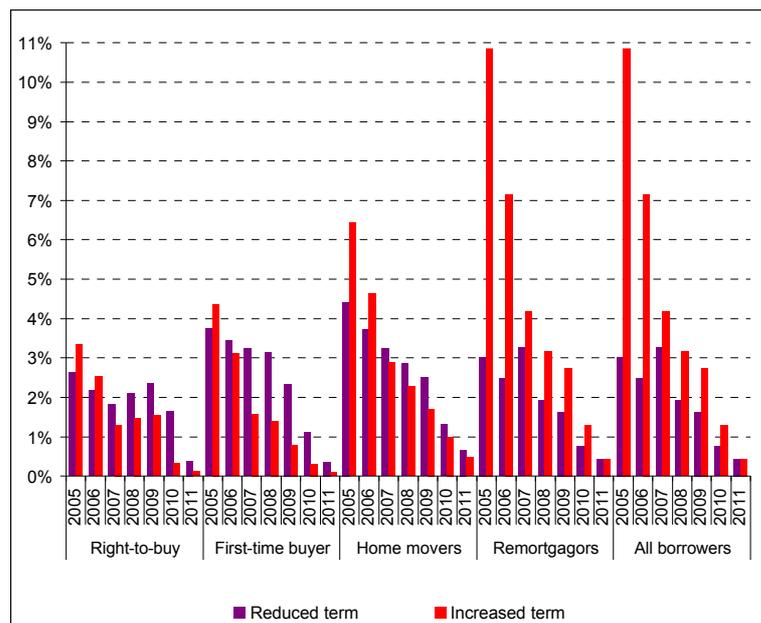


Note: (1) Data on all borrowers up to 1995 excludes remortgages; (2) Data on mortgage terms in 2003-2004 is not available.

Source: SBS, SML, FSA PSD

- Our analysis of regulated mortgages sold between 2005-2010 shows that most mortgage borrowers continued with the same mortgage term that they had taken at origination.
- For example, of the borrowers who took out mortgages in 2005, by March 2012, 86% were on the same term, 11% had increased their term and 3% decreased their term.
- It also follows from the data that, on balance, borrowers were more likely to have increased their term.
- Remortgagors (as classified at origination) were more likely than any other borrower type to have increased their term.

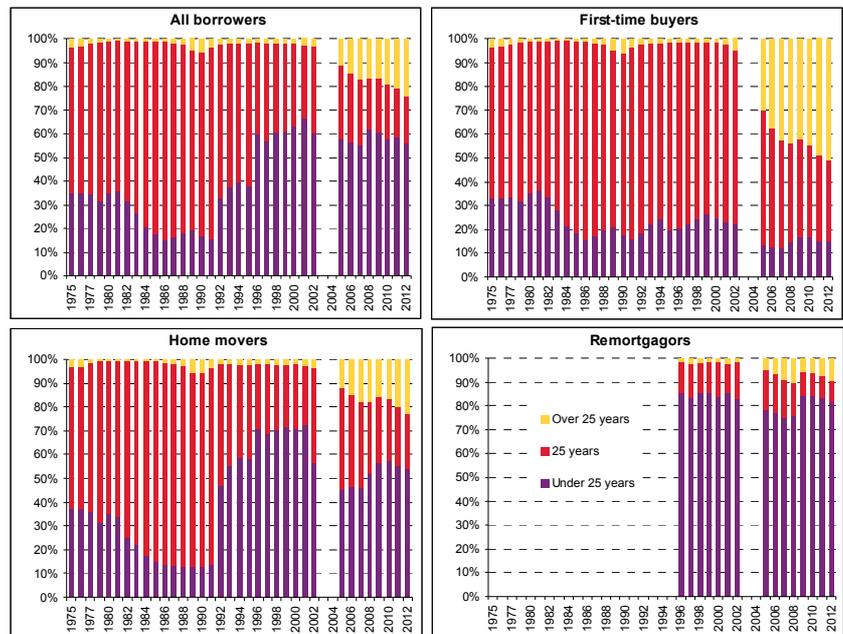
Exhibit 12.3: Proportion of borrowers who reduced or increased their mortgage term, by year of mortgage sale and borrower type



Note: As at March 2012

Source: PSD Performance data 2012

- Overall, in recent years there has been a proportional increase in the sales of mortgages with longer terms (26+ years), at the expense of a 'staple' 25-year mortgage, which has dominated the market over the past three decades.
- In Q1-Q2 2012, 24% of new mortgages had terms in excess of 25 years.
- This trend could be explained by demographic changes (people working longer) or by affordability considerations (taking out longer terms in order to reduce mortgage payments).
- The trend for longer-term mortgages was mainly driven by FTBs. In Q1-Q2 2012, only 34% chose a staple 25-year mortgage, while 51% chose terms in excess of 25 years, and 15% went for terms under 25 years.
- A quite different trend is observed amongst former owner occupiers (remortgagors and home movers). While the sales of longer-term mortgages to this group have also increased, in Q1-Q2 2012, only 23% of home movers and 9% of remortgagors had mortgage terms in excess of 25 years, and 54% and 82% respectively had terms below 25 years.

Exhibit 12.4: Trend in sales of longer- and shorter-term mortgages

Note: (1) Data on all borrowers up to 1995 excludes remortgages; (2) Data on mortgage terms in 2003-2004 is not available.

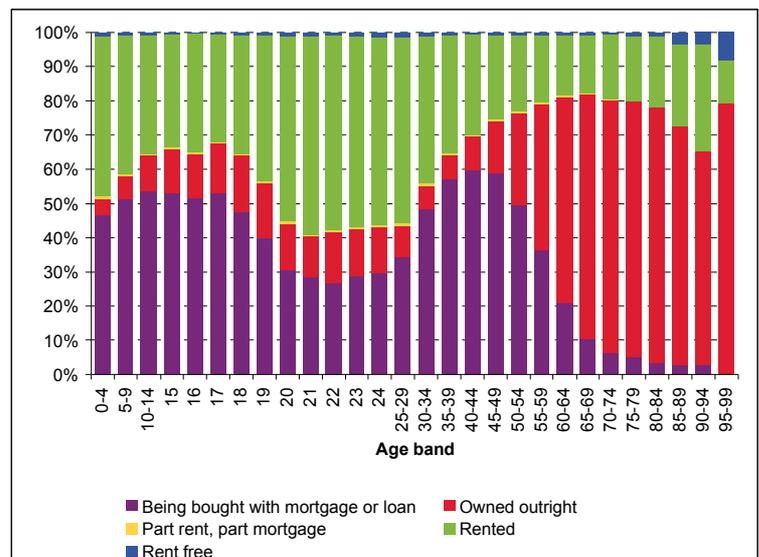
Source: SBS, SML, FSA PSD

13

Mortgage borrowing and borrowers' age

- In the UK, over 50% of adults aged 35 to 54 and over 50% of children up to 18 live in households where there is a mortgage.
- Understandably, ownership with a mortgage decreases with age as borrowers pay off their mortgages and become outright home owners.
- Only a small proportion of elderly consumers have a mortgage. According to DCLG, under 3% of 75+ year olds have a mortgage.¹⁷

Exhibit 13.1: Tenure, by age of occupant

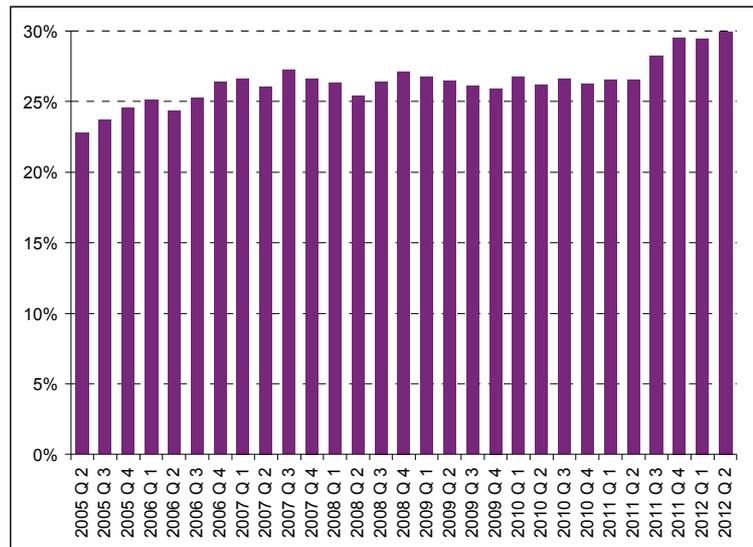


Source: Quarterly Labour Force Survey, January - March, 2012

¹⁷ Some of these mortgages could be lifetime mortgages. See Chapter 21 for more information on lifetime mortgages.

- In the past seven years, around 26% of all regulated mortgages were sold to borrowers with an expectation that the borrower would continue repayments after the age of 65.
- This could indicate that lenders believe that borrowers have sufficient income in retirement or will remain in employment and be able to continue to meet their mortgage payments.

Exhibit 13.2: Proportion of mortgages extending into retirement

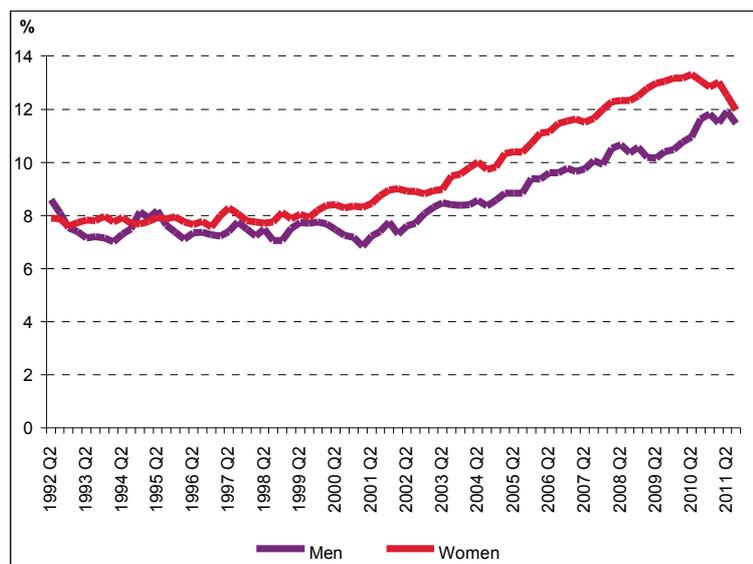


Note: We made an assumption that the mortgage extends into retirement if the expected age at redemption is 65 or older.

Source: FSA PSD

- However, according to the ONS data, only 11.5% of men continued working after the age of 65 and 12% of women continued working after the age of 60, so many of the remaining households are likely to have experienced a decrease in income.

Exhibit 13.3: Employment rates at 65+ for men and 60+ for women

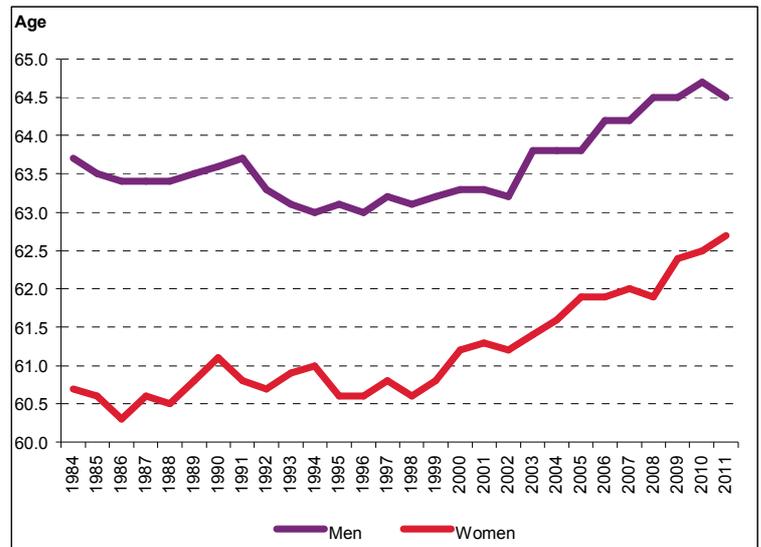


Note: Three-month rolling quarters; not seasonally adjusted

Source: Labour Force Survey, ONS

- In 2011, the average retirement age for men was 64.5 and the average retirement age for women was 62.7.
- However, the proportion of older age groups in employment has been increasing steadily over the past ten years. It is possible that this trend will continue following the recent changes to state retirement age.

Exhibit 13.4: Average age of withdrawal from the labour market in the UK, by gender

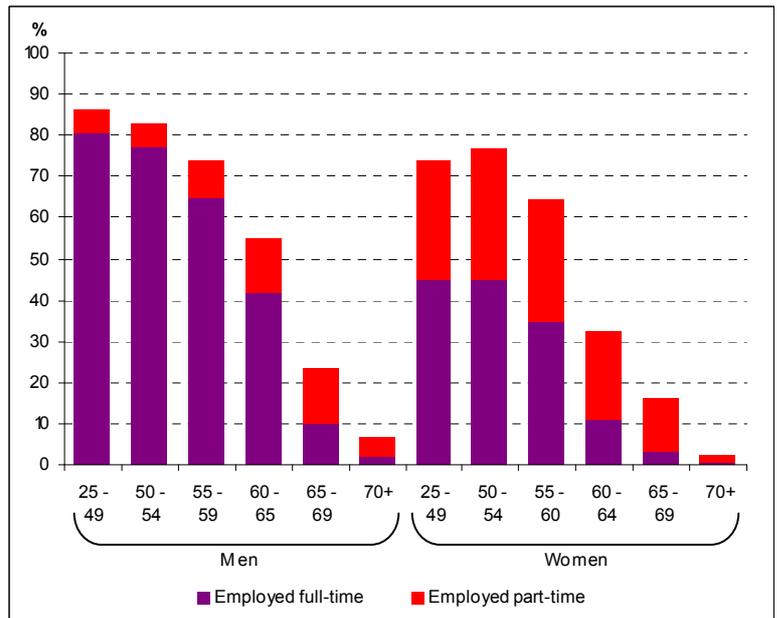


Note: Annual data for period 1984 -1991, April to June data for period 1992-2011; data not seasonally adjusted.

Source: Labour Force Survey, ONS

- According to the ONS, in 2011, of 65-69 year-old men, 10% worked full-time and 13.2% worked part-time and of 70+ year-old men, 2% worked full-time and 4.6% worked part-time.
- For 65-69 year-old women, 3.5% worked full-time and 12.6% worked part-time and of 70+ year-old women, 0.4% worked full-time and 2% worked part-time.

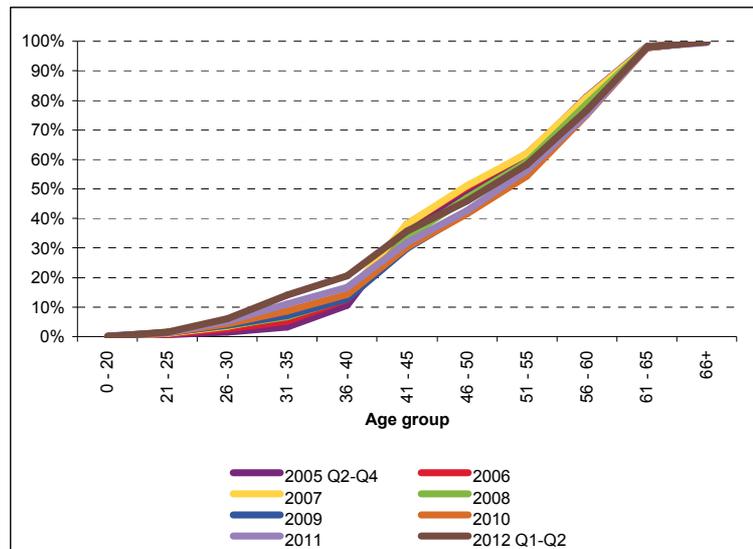
Exhibit 13.5: Full-time and part-time employment, by age and gender



Source: Labour Force Survey, ONS

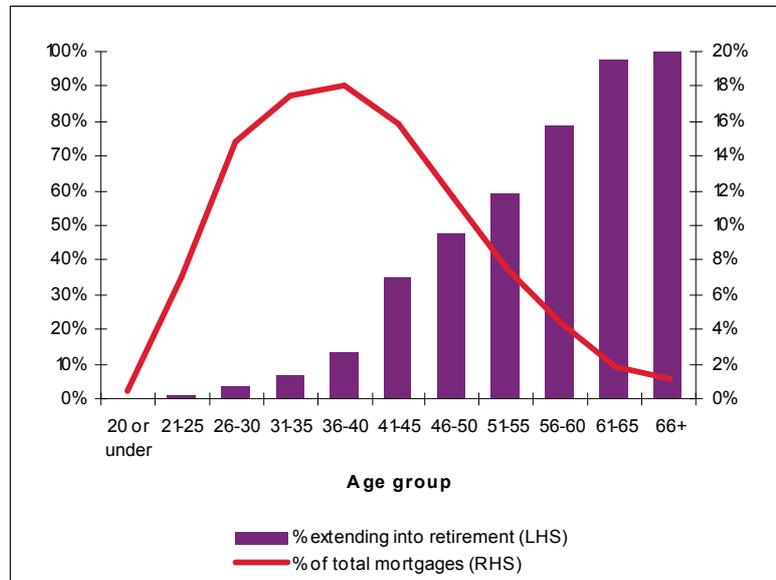
- The proportion of lending extending into retirement has remained relatively stable over the past six years, although there was some increase in the run-up to the credit downturn of 2007.
- Taking into account minor changes in borrower age over this period, in the more recent years (2009-2012), lenders were slightly more likely to sell mortgages extending past the age of 65 to younger borrowers and slightly less likely to older borrowers.
- This reflects changes in retirement age, with younger borrowers now expected to work longer. It may also reflect the changes in the risk profile of lending over this period, which led to a reduction in lending to older borrowers whose retirement is closer.
- Older borrowers, however, were much more likely to have mortgages extending past the age of 65 in all periods for which we have data.

Exhibit 13.6: Lending into retirement, by year of sale and age group



Source: FSA PSD

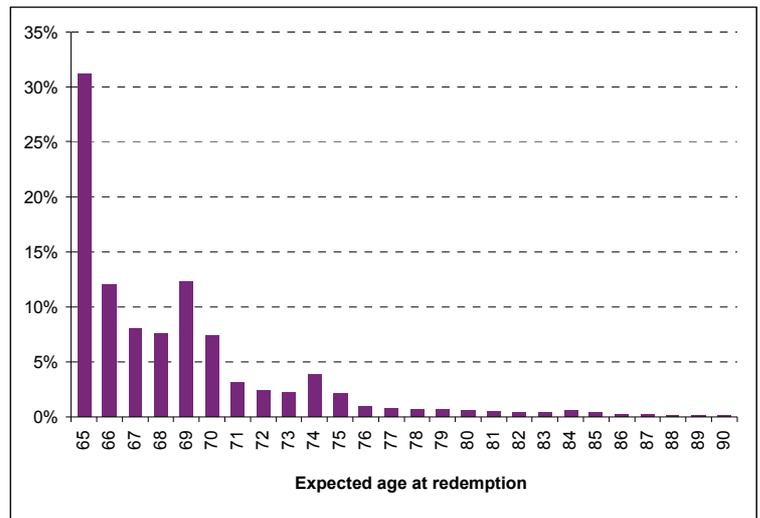
Exhibit 13.7: Proportion of mortgages extending into retirement, by age group (April 2005 – June 2012)



Source: FSA PSD

- Most mortgages extend into retirement by just a few years – 78% are expected to be paid off by the time the borrower is 70 years old.
- However, 5% are expected to be paid off after the borrower is 80 years or older.

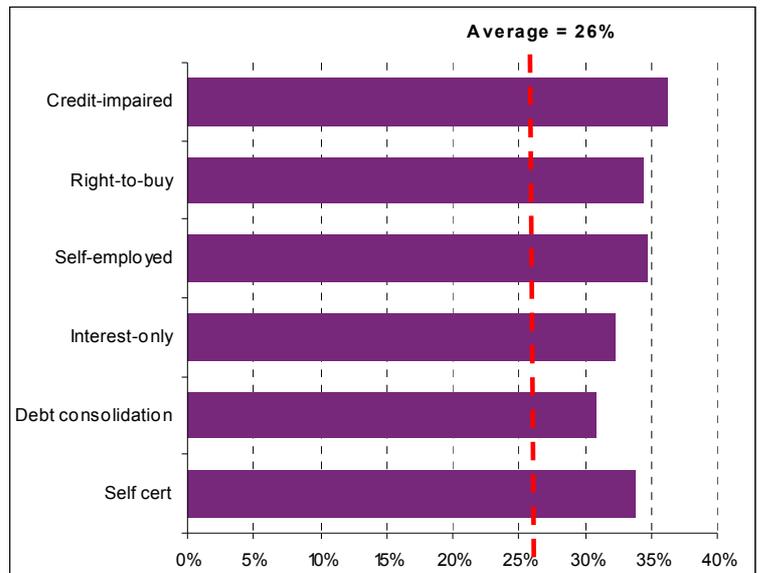
Exhibit 13.8: Expected age at redemption for borrowers whose mortgages extend into retirement (April 2005 – June 2012)



Source: FSA PSD

- Our data shows that some borrower types were more likely than others to borrow into retirement. However, in some cases the differences we see simply reflect the fact that some types of borrowers are, on average, older than others.

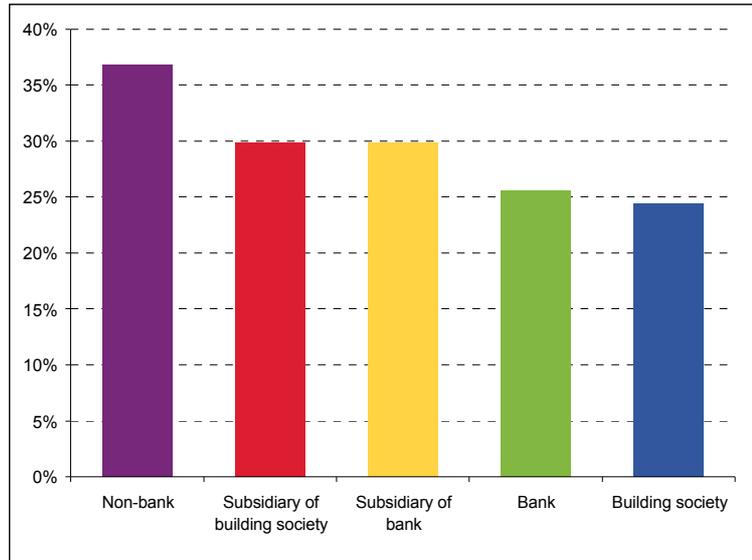
Exhibit 13.9: Lending into retirement on selected products (April 2005 – June 2012)



Source: FSA PSD

- Some types of lenders, notably those that serviced higher-risk borrowers, were also more likely to lend into retirement.

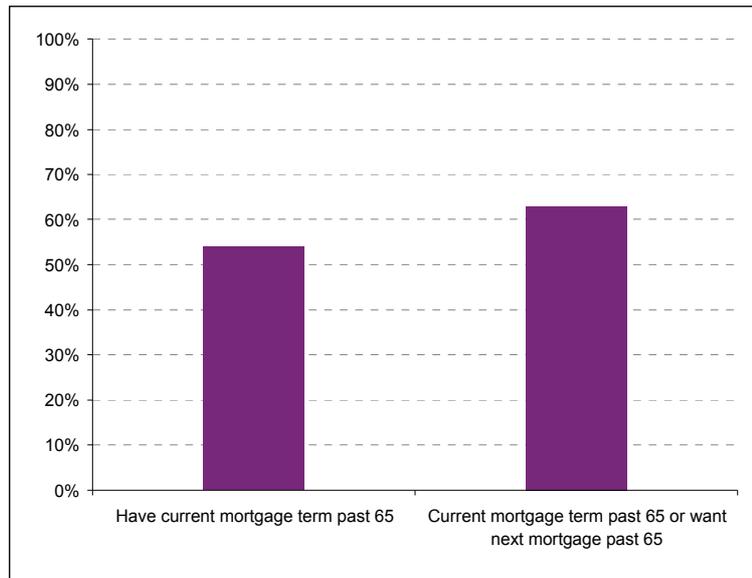
Exhibit 13.10: Proportion of mortgages extending into retirement, by type of lender (April 2005 – June 2012)



Source: FSA PSD

- According to the Policis survey, a significant proportion of borrowers over 50 have mortgages that already extend into retirement, or want their next mortgage to extend into retirement.

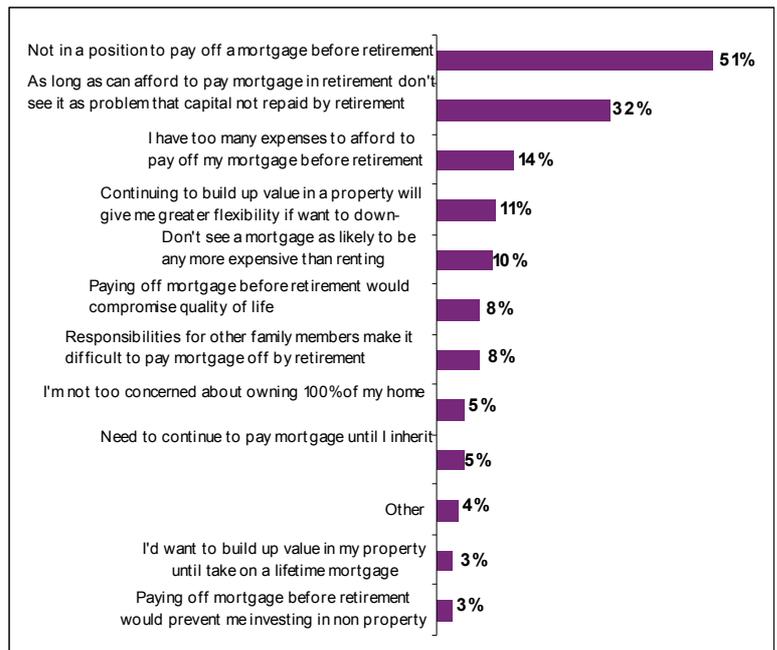
Exhibit 13.11: Mortgagors over 50 - by whether they have or want mortgage term past age 65



Source: Policis

- This is mainly because these borrowers are not in a position to repay their mortgages by retirement.

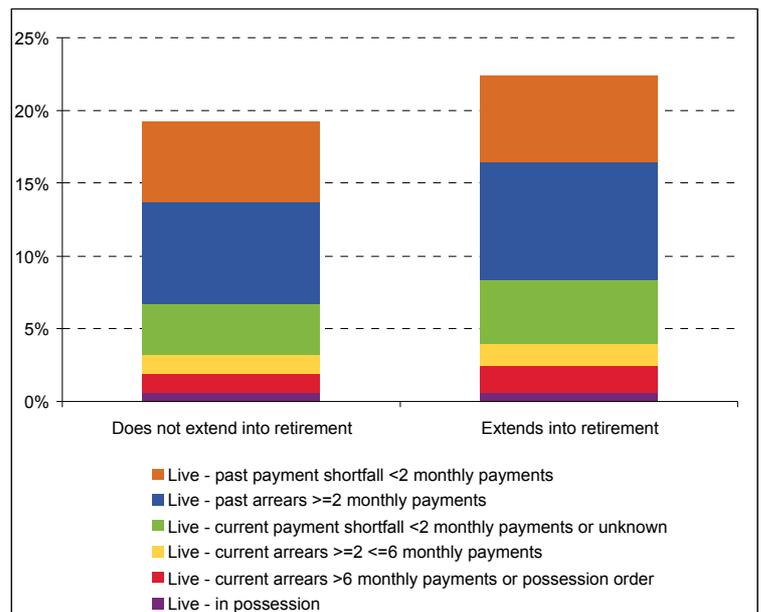
Exhibit 13.12: Reasons for wanting a mortgage stretching past age 65



Source: Policis

- The risk of lending into retirement is that the borrower may not be able to afford mortgage payments later in life if their income reduces.
- From our data, we do observe a higher record of payment problems for those borrowers whose mortgages extend into retirement.
- This could be because some borrowers may have stretched affordability by taking mortgages for longer (thus extending into retirement).

Exhibit 13.13: Mortgage performance, if mortgage extends into retirement

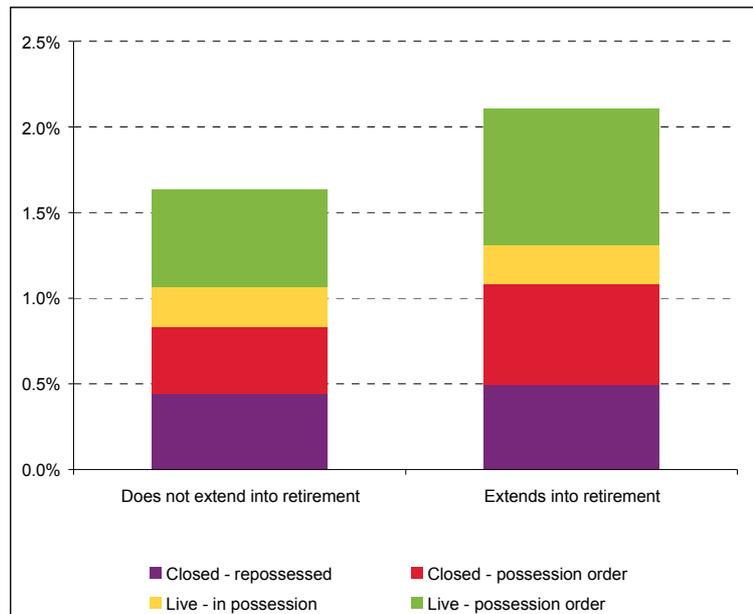


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- The same applies for repossessions. Borrowers whose mortgages extend past retirement age are more likely to have their properties repossessed.
- Again, this could be a reflection of the fact that some borrowers stretch affordability by taking mortgages for a longer term.

Exhibit 13.14: Mortgage repossessions, if mortgage extends into retirement

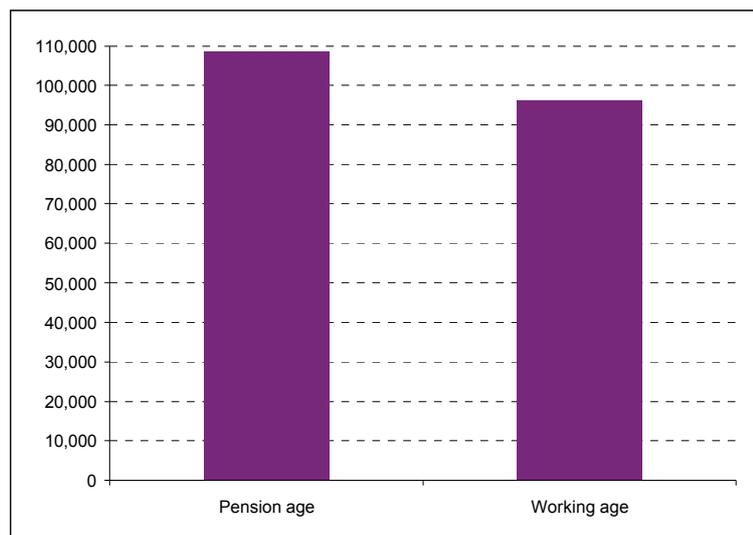


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 – December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- The data from the Department for Work and Pensions (DWP)¹⁸ suggests that 53% of people claiming Support for Mortgage Interest benefit (SMI) are retired.
- As of May 2011 205,000 people claimed SMI, of whom 108,700 were retired.
- The average weekly payment to those aged 60-64 was £26 and to those aged 65+ was £18.

Exhibit 13.15: Support for Mortgage Interest benefit: number of claimants as of May 2011



Source: DWP

¹⁸ See DWP's Support for Mortgage Interest – call for evidence – Impact Assessment at www.dwp.gov.uk/docs/support-for-mortgage-interest-call-for-evidence-ia.pdf

14

A closer look at self-employed borrowers

- ONS reports that there was an increase in the proportion of self-employed in the UK in the 1980s.
- Changes to the tax system targeted at supporting small businesses may have contributed to this trend.
- From the 1990s, the proportion of self-employed in the total economically active population remained flat at around 12%.

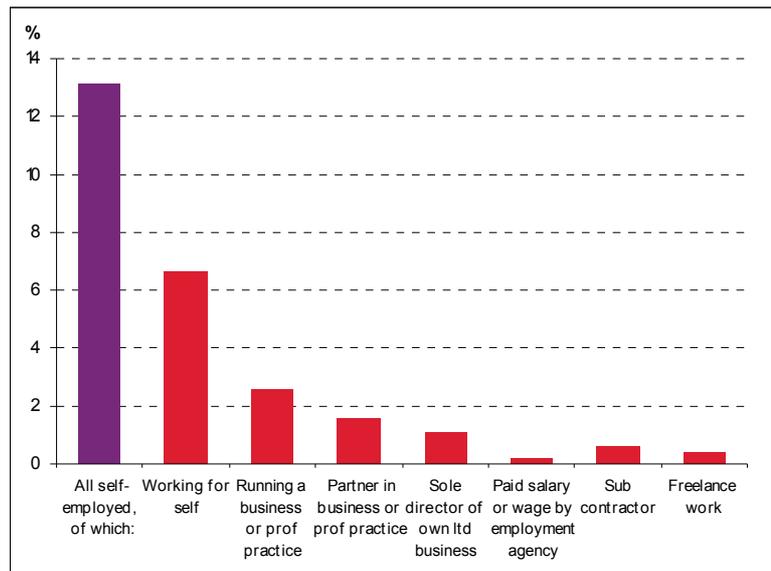
Exhibit 14.1: Proportion of self-employed in total economically active population



Source: Labour Force Survey (1995-2003), Annual Population Survey (2004-2012), Nomis

- At present, the self-employed account for just over 13% of all economically active individuals living in households where there is a mortgage.
- The self-employed is a diverse group. Just over half of all self-employed mortgage borrowers (51%) are sole traders; 40% run limited companies or are partners in businesses and practices; and a further 9% work as subcontractors, agency workers or freelancers.

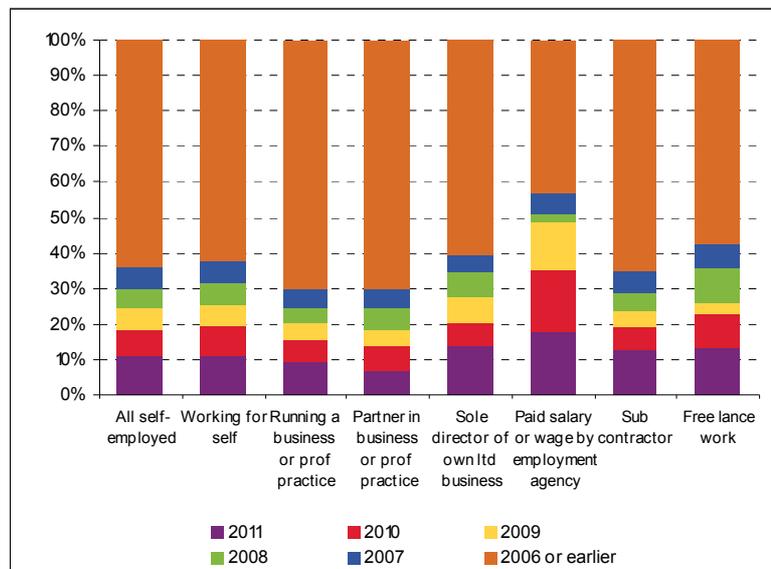
Exhibit 14.2: Self-employed mortgage borrowers by type, as % of all mortgage borrowers



Source: Quarterly Labour Force Survey, January - March, 2012

- Most self-employed mortgage borrowers have been running their businesses for a long time.
- Overall, 64% have been in their current business for over five years. Only around 18% started their business less than two years ago.

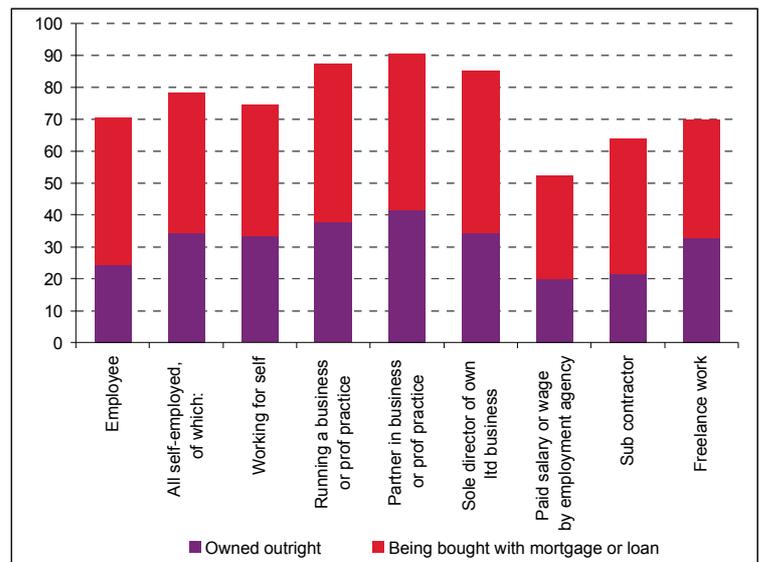
Exhibit 14.3: Self-employed mortgage borrowers, by type of self-employment and year when business started



Source: Quarterly Labour Force Survey, January – March 2012

- Proportionally, self-employed borrowers are more likely than employed borrowers to own their home and are less likely to have a mortgage secured on it. However, this may simply reflect the fact that, on average, self-employed borrowers are older.
- The level of home ownership, including with a mortgage, varies quite considerably depending on the type of self-employment.
- Nearly 90% of self-employed borrowers who run limited companies, or are partners in businesses and practices are home owners, compared with 52% of agency workers.

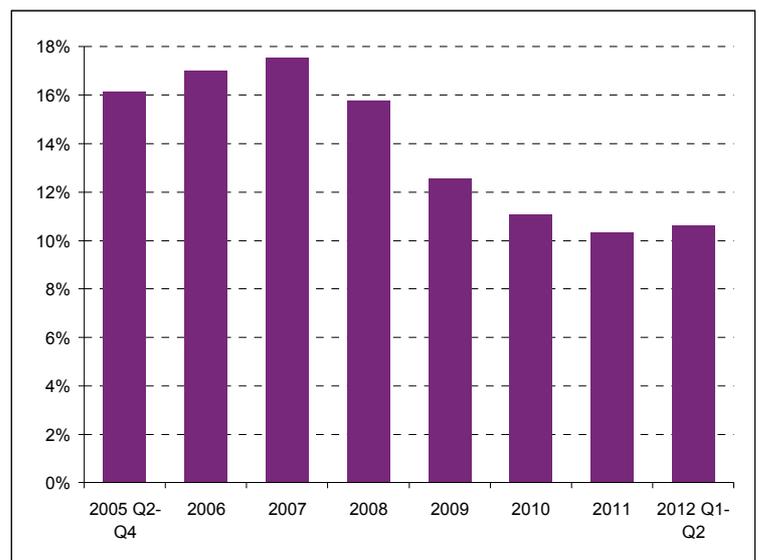
Exhibit 14.4: Home ownership by type of employment: owning outright and with a mortgage



Source: Quarterly Labour Force Survey, January – March, 2012

- At the peak of the market, self-employed borrowers accounted for a greater proportion of sales than the share of the self-employed in the population would suggest.
- This could have been for a number of reasons. Some self-employed borrowers (e.g. sole traders) may have used mortgage equity withdrawal to finance their businesses.
- It is also possible that some borrowers may have misreported their employment status as self-employed to access self-certification mortgage products.
- The proportion of new mortgage sales to self-employed borrowers at the market height in 2007 was just under 18%, and has since gradually reduced to account for around 11% of the total today.
- This is because lenders have reduced lending to higher-risk self-employed borrowers, as part of a general tightening of lending criteria following the downturn.

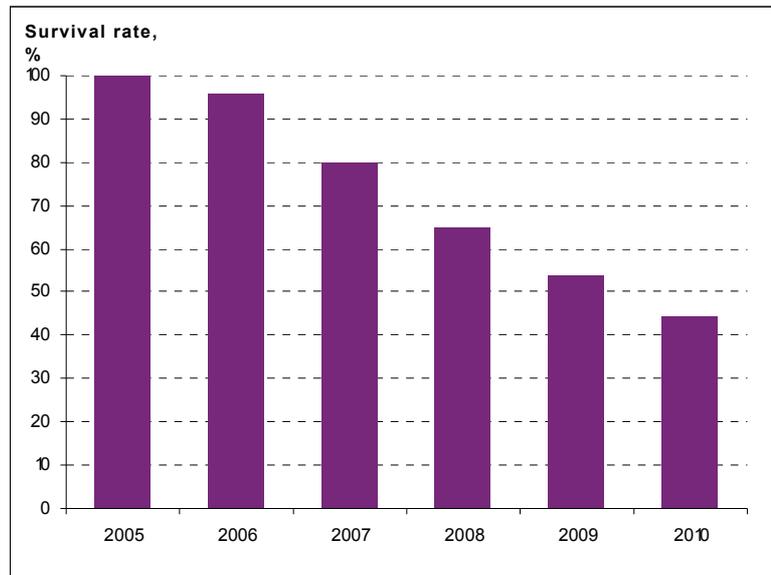
Exhibit 14.5: Proportion of mortgage sales to self-employed in total mortgage sales



Source: FSA PSD

- Self-employed borrowers tend to be higher-risk than employed borrowers simply because their income is more volatile. Also, for self-employed borrowers who are sole traders, personal finances are often mixed with business finances, so it is easier for them to accumulate and default on debts.
- For newly established ventures, survival rates are quite low (only 44% survive for five years).
- In 2007, nearly 30% of all credit-impaired borrowers were self-employed compared with 17% of borrowers with a clean credit history.

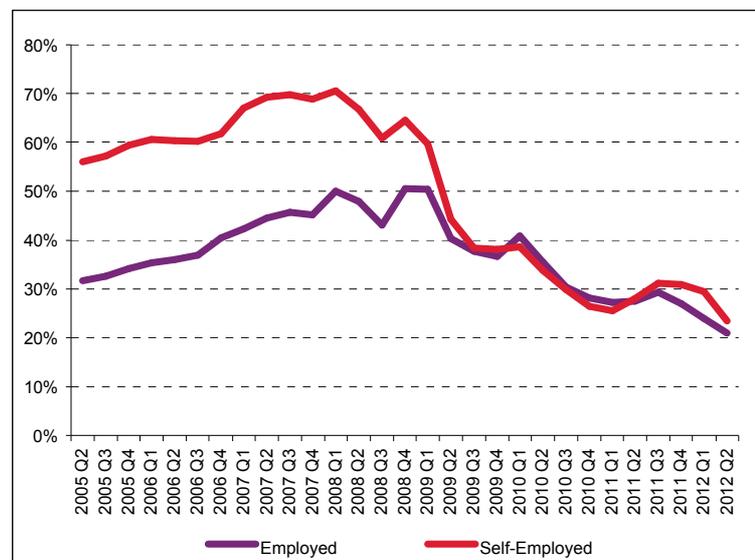
Exhibit 14.6: Survival rates of businesses born in 2005



Source: ONS

- At the peak of the market, most mortgages to self-employed borrowers were made with no verification of income.
- There was a significant change following the market downturn and tightening of lending criteria.
- In 2010-H1 2012, a much smaller proportion of mortgages were advanced on an income non-verified basis, and lenders were about as likely to verify the incomes of the self-employed as they were of the employed.

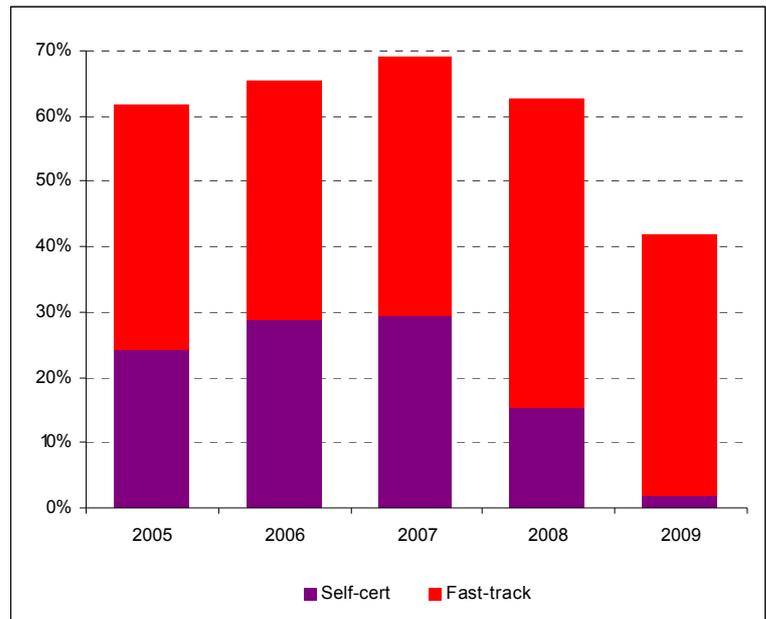
Exhibit 14.7: Mortgage sales with non-verified income, by employment status



Source: FSA PSD

- Although we do not have comprehensive data on self-certification of income and the true size of this market is unknown, we estimate that around 30% of self-employed borrowers may have self-certified their income in the run up to the crisis.

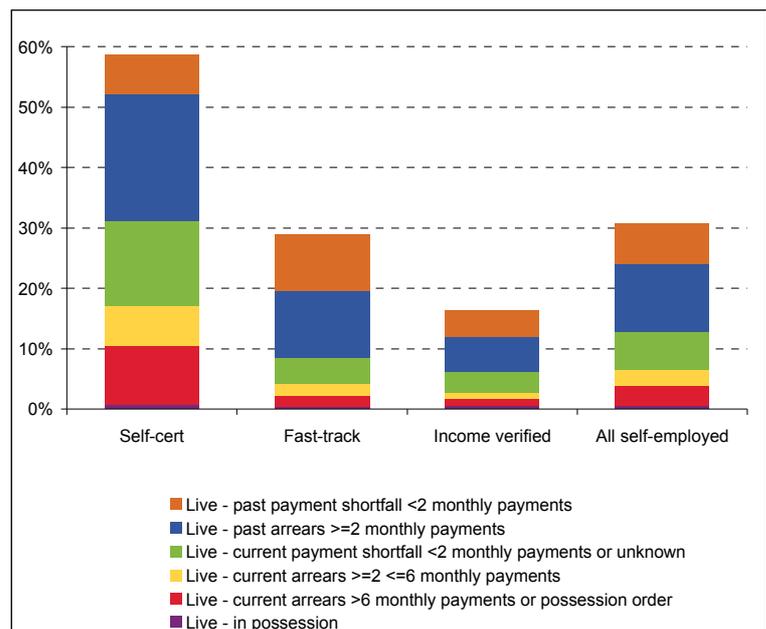
Exhibit 14.8: Income non-verified mortgages to self-employed: fast tracked and self-certification mortgages



Source: PSD Performance data 2011

- Of course, not all self-employed borrowers who chose to self-certify would have exaggerated their incomes. However, the arrears figures suggest that some did.
- We estimate that around 59% of self-certified mortgages to self-employed borrowers that are still outstanding have a record of payment problems.
- Of those, 31% have current missed payments, of which 17% are at least two months behind.

Exhibit 14.9: Performance of mortgages to self-employed, by type of income verification

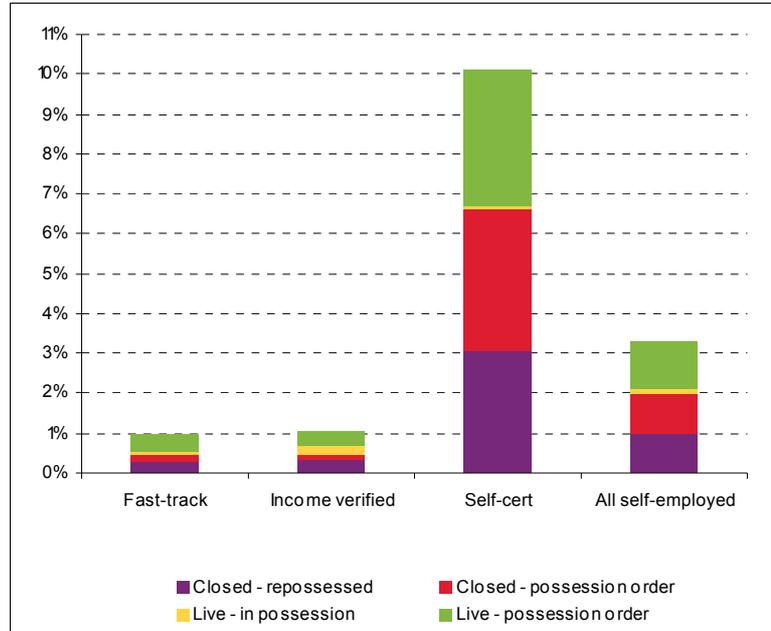


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Of all sales to self-employed borrowers between April 2005 and December 2011, approximately one in 30 borrowers have had their homes repossessed or had a possession order made against their property.
- The figures are much higher where the mortgage was self-certified, with one in 10 borrowers having been repossessed or had a possession order made against their property.

Exhibit 14.10: Repossessions on mortgages to self-employed, by type of income verification

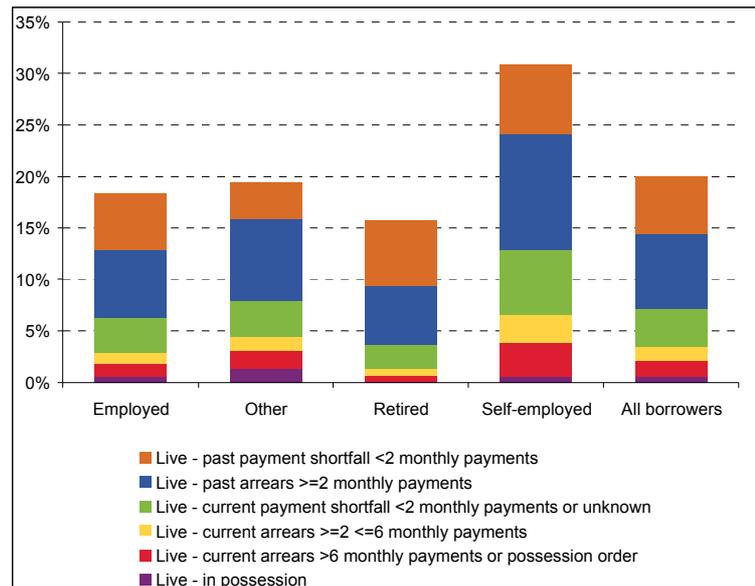


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Overall, the mortgage accounts of self-employed borrowers perform worse than those of employed borrowers.

Exhibit 14.11: Mortgage performance, by type of employment

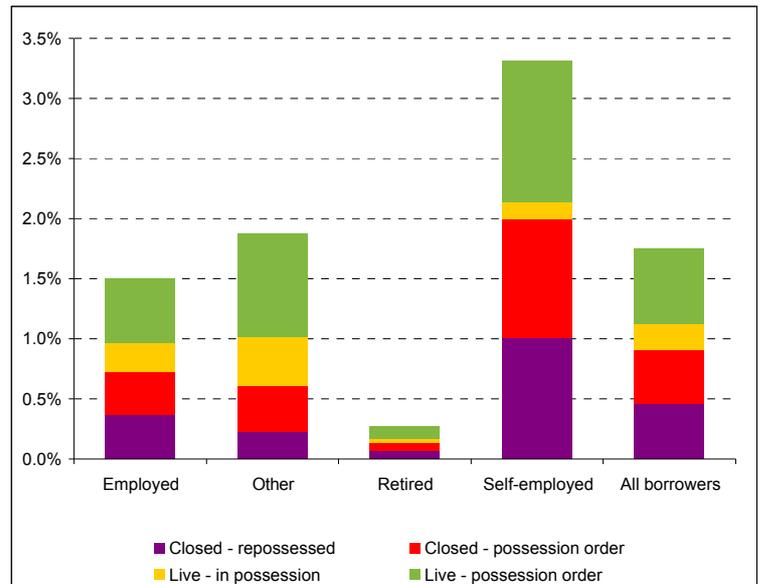


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Self-employed borrowers are more likely than employed borrowers to have their homes repossessed.

Exhibit 14.12: Mortgage repossessions, by type of employment



Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Even in the absence of other risk factors, self-employed borrowers are almost three times as likely as employed to be in arrears of two months or more and twice as likely to have their property repossessed (if we compare risk types one and three from our risk combinations matrix).
- The performance of self-employed mortgages greatly deteriorates when there are other risks involved, for example, credit impairment, debt consolidation, RTB or borrowing at high LTV.

Exhibit 14.13: Risk combinations and mortgage performance, self-employed

Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of sales	Outstanding mortgages			All sales Total: possessions and possession orders
							Total: any record of missed payments	Total: current missed payments or arrears	Total: current arrears 2+ months	
1	NO	NO	NO	NO	NO	53.5%	13.6%	3.3%	1.1%	0.4%
3	NO	NO	YES	NO	NO	9.1%	22.6%	7.0%	3.1%	1.0%
7	NO	NO	YES	YES	NO	0.5%	38.0%	15.3%	7.6%	1.8%
8	NO	YES	YES	NO	NO	4.2%	38.5%	18.6%	10.1%	5.9%
10	NO	NO	YES	NO	YES	0.1%	44.7%	16.9%	8.6%	4.7%
11	NO	YES	YES	YES	NO	0.2%	56.5%	29.7%	16.6%	7.6%
13	NO	YES	YES	NO	YES	0.0%	61.0%	29.7%	18.5%	12.1%
16	YES	NO	YES	NO	NO	0.4%	75.3%	44.4%	26.0%	12.0%
19	YES	NO	YES	YES	NO	0.1%	81.6%	48.8%	26.8%	9.6%
20	YES	YES	YES	NO	NO	0.3%	81.9%	53.7%	34.6%	21.3%
22	YES	YES	YES	NO	YES	0.0%	85.0%	50.4%	32.5%	26.6%
23	YES	YES	YES	YES	NO	0.1%	86.6%	56.4%	33.2%	17.6%
24	YES	NO	YES	NO	YES	0.0%	88.6%	49.5%	23.8%	13.7%
Total						100.0%	20.0%	7.1%	3.4%	1.8%

Note: this is an extract from the full illustration on risk combinations in Exhibit 6.9.

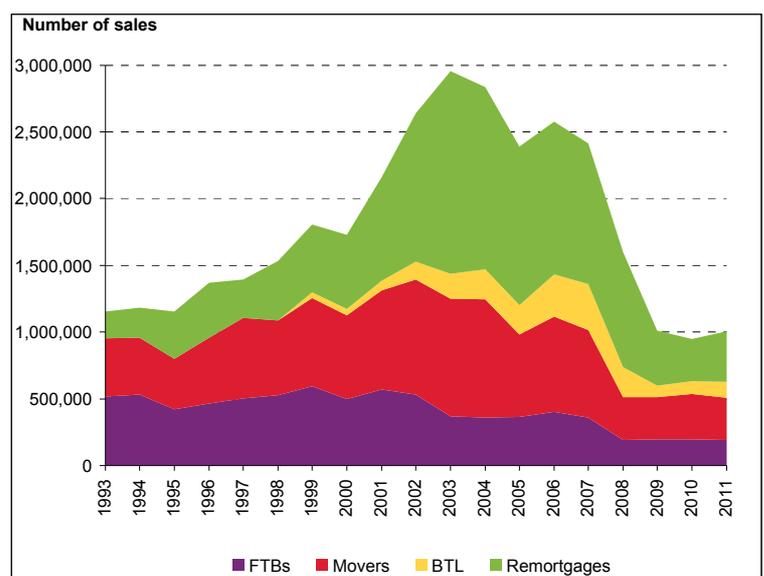
Source: PSD Performance data 2012

15

A closer look at first-time buyers

- In the 1990s, around 500,000 mortgages per year were to first-time buyers (FTB). But sales to FTBs have been decreasing over the past ten years:
- Some FTBs have been priced out of the market by increasing house prices.
- Some have been out-competed by buy-to-let investors, chasing the same properties.
- Most recently (2008 onwards), some have had to delay buying a property to save for the larger deposits required by lenders, following the tightening of lending criteria in response to funding constraints.
- Also more recently, demand for mortgages by FTBs may have declined on the expectation that house prices would fall further and that properties would become more affordable.
- Currently, economic conditions and uncertainty of pay and employment are also likely to deter some potential FTBs from taking out mortgages.

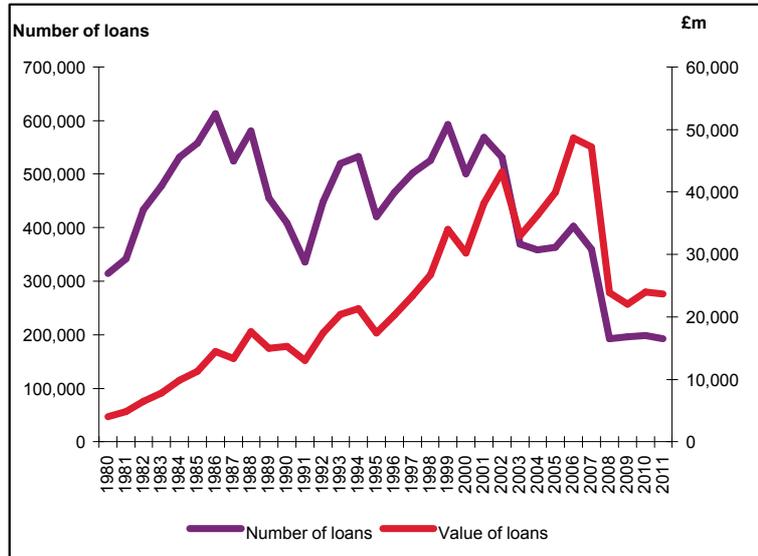
Exhibit 15.1: Mortgage lending by purpose – number of sales



Source: CML

- Although in terms of the number of sales, mortgage lending to FTBs has been decreasing from the late 1990s, in terms of value, there was a steady increase until the market downturn in 2008.
- In 1997, there were over 500,000 mortgage sales to FTBs with a total value of just over £23m, at an average of £46,500 per advance.
- By contrast, in 2007, there were just under 360,000 mortgage sales to FTBs (nearly 30% fewer than in 1997), but the total value of those loans was over £47m (over 100% more than in 1997), at an average of £131,000 per advance.

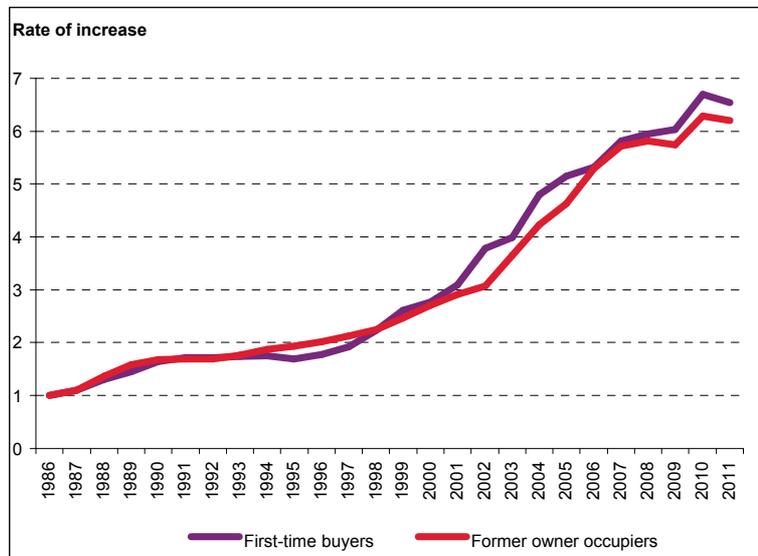
Exhibit 15.2: Volume and value of new lending to first-time buyers



Source: CML

- The increase in the value of lending to FTBs was driven from the late 1990s by the increase in house prices.
- In fact, in relative terms, the prices of the cheaper properties targeted by FTBs increased somewhat more than the prices of the more expensive properties favoured by former owner-occupiers.
- The increase in the prices of properties attractive to FTBs may have been fuelled by buy-to-let investors who targeted the same type of properties.
- Today, the average FTB is 31 years old, earns around £34,000 and borrows at 72% LTV (but can borrow up to 95% at a higher cost).
- The average buy-to-let investor is between 45 and 64 years old, is a higher-rate taxpayer and borrows at 55% LTV (but can borrow up to 80%).
- Overall, this puts a typical buy-to-let investor in a more favourable position in terms of affordability and access to finance.

Exhibit 15.3: House price change, by type of buyer

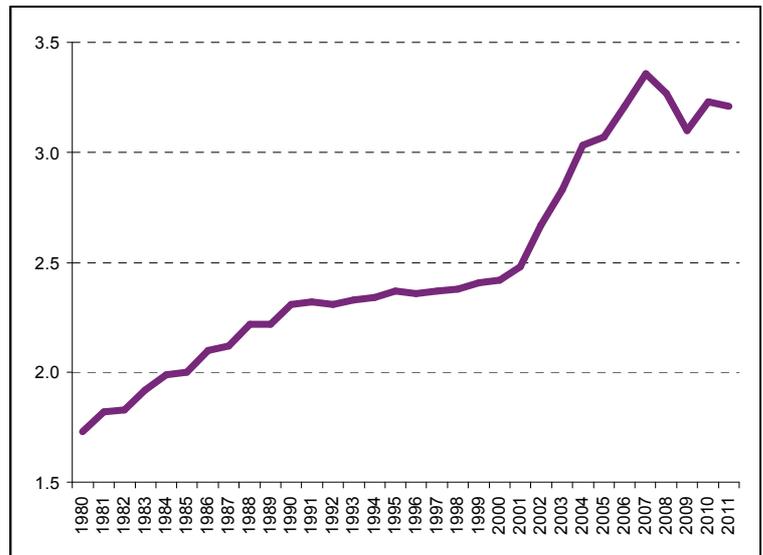


Note: Baseline 1986 = 1

Source: DCLG, ONS

- As a result of house price increases, the average income multiple required by first-time buyers, which stood at 2.5 times salary just ten years ago, increased to nearly 3.5 times salary by 2007.

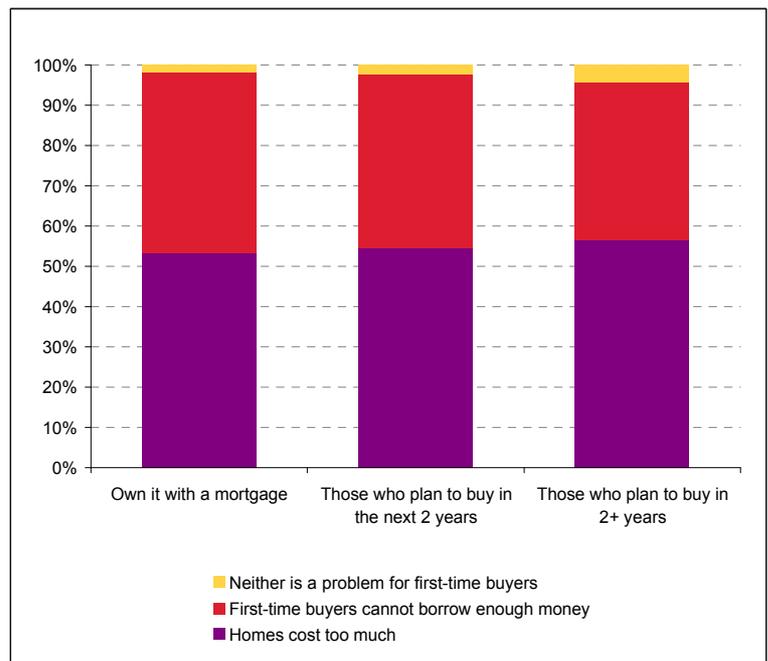
Exhibit 15.4: Median loan multiple of first-time buyers



Source: CML

- According to the 2011 YouGov survey for Shelter, high house prices is the main reason why FTBs are not entering the housing market.

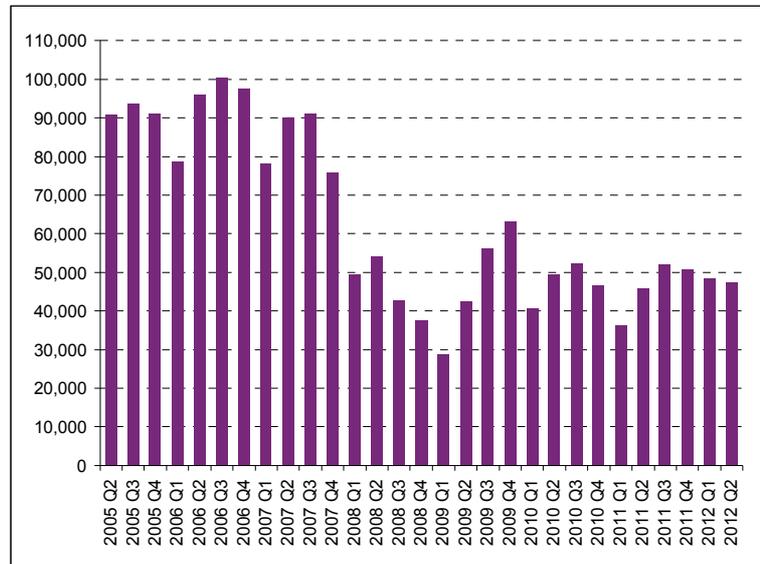
Exhibit 15.5: Thinking about first-time buyers - which do you think is a bigger problem



Source: YouGov online survey for Shelter (GB representative, 2,065 respondents, April 2011), FSA analysis

- Following the market downturn, mortgage sales fell, including the sales to FTBs.

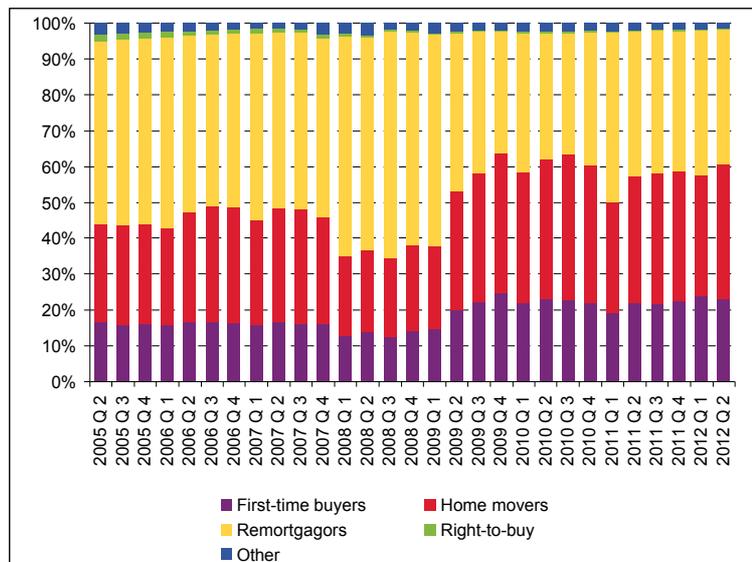
Exhibit 15.6: Number of mortgage sales to first-time buyers



Source: FSA PSD

- Currently, the proportion of mortgage sales to FTBs is actually higher than pre-crisis and stands at 23% of all regulated sales (although in absolute terms, the number of sales to FTBs has decreased).
- This is mainly because of the decrease in remortgaging, which accounted for 61% of all mortgage sales in 2008, but for just 39% in Q1-Q2 2012.

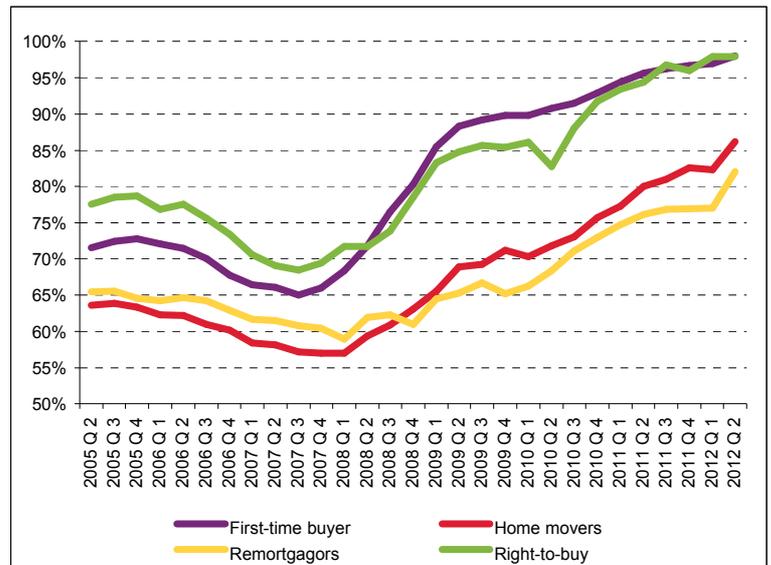
Exhibit 15.7: Structure of regulated mortgage sales, by type of borrower



Source: FSA PSD

- FTBs tend to take out repayment mortgages.
- However, pre-crisis, a large proportion of FTBs took out interest-only mortgages, most likely to reduce monthly payments (see also Exhibit 11.7).

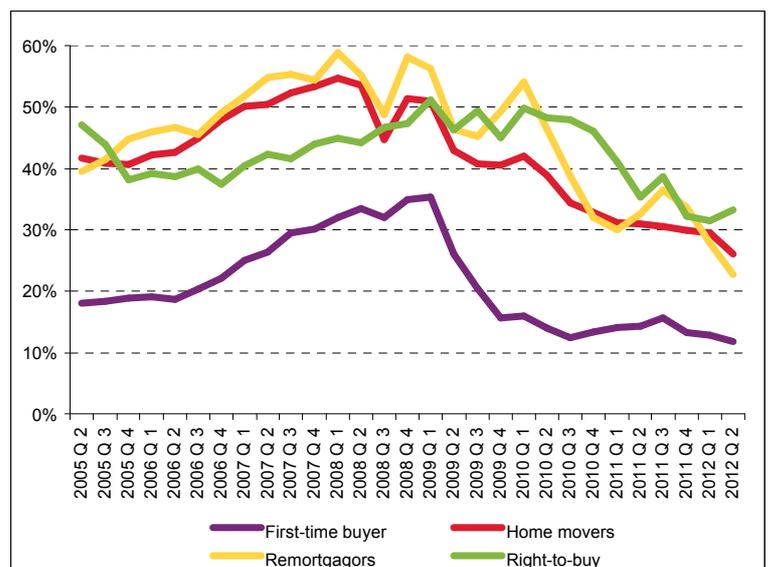
Exhibit 15.8: Proportion of borrowers with repayment mortgages, by borrower type



Source: FSA PSD

- Lenders are more likely to verify the income of FTBs than of other borrowers.
- Yet, in 2007 to early 2009, nearly 35% of mortgages to FTBs were granted without checking income.

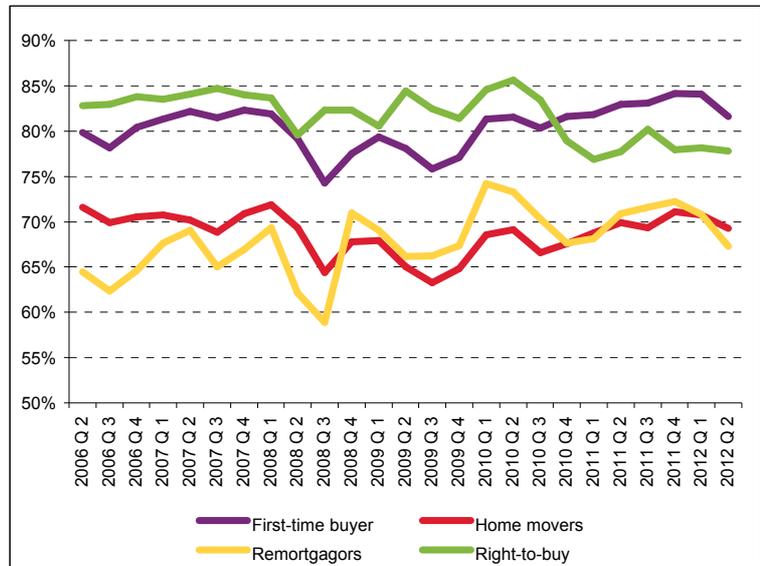
Exhibit 15.9: Proportion of mortgages where income was not verified, by borrower type



Source: FSA PSD

- Most FTB mortgages – around 80% – are sold with advice.

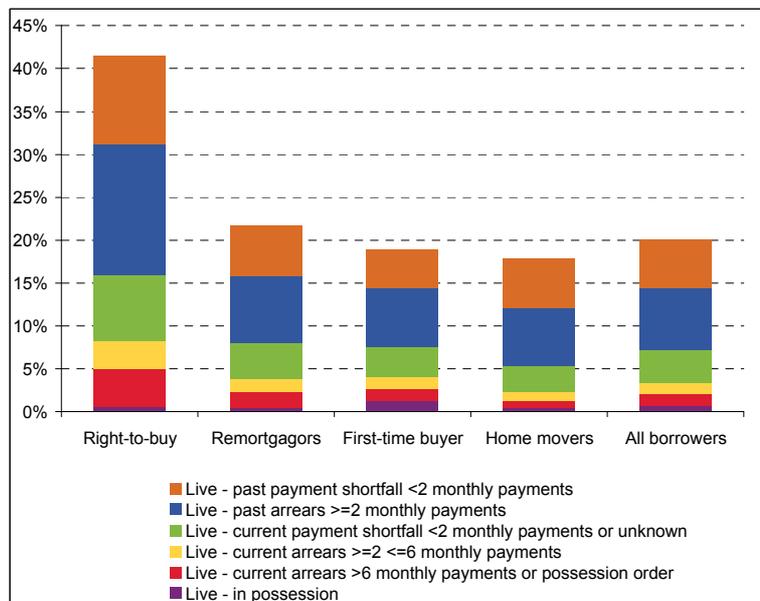
Exhibit 15.10: Provision of advice, by type of borrower



Source: FSA PSD

- FTB mortgages perform better than those of remortgagors and marginally worse than those of home movers.

Exhibit 15.11: Mortgage performance, by type of borrower

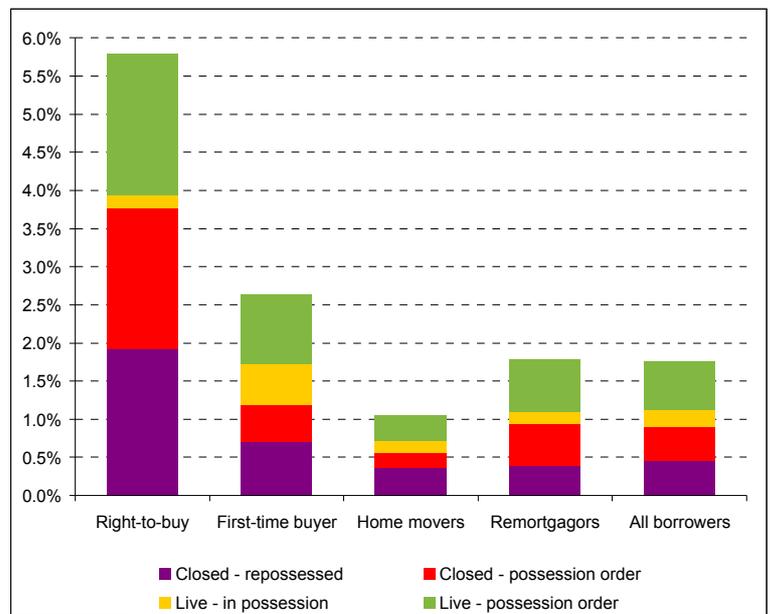


Note: This Exhibit shows performance of mortgages sold in April 2005 – December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- FTBs are, however, considerably more likely than movers and remortgagors to have their home repossessed.
- Of those FTBs who bought their homes in the period 2005 - 2011, one in 40 have been repossessed or have had a possession order made against their property.
- This is mainly because, on average, FTBs are more likely than other borrower types to take mortgages at high LTVs, where it may be in the interests of lenders and borrowers to start the possession process more quickly to minimise the potential loss on sale.

Exhibit 15.12: Mortgage repossessions, by type of borrower

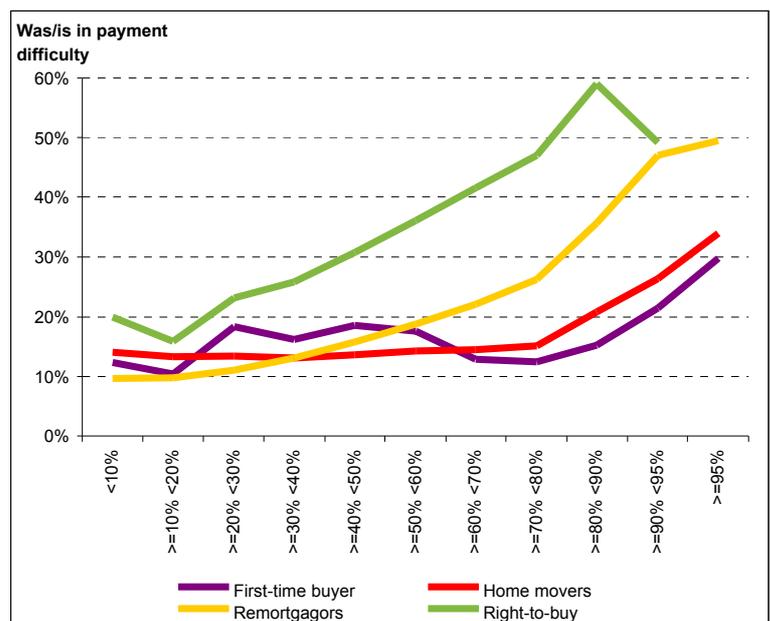


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 – December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Yet the mortgages of FTBs perform better than those of other borrower types at higher LTV bands.
- Poorer performance of FTB mortgages at lower LTV bands could be due to smaller sample sizes (as most sales to FTBs are at higher LTVs). It is also possible that some lenders who report PSD may have misclassified some RTB borrowers as FTBs. Although, technically, RTB borrowers buying their home for the first time could be considered first-time buyers, for reporting purposes in PSD we treat them separately.
- Another possible explanation for the poorer performance of FTB mortgages at lower LTVs, in comparison with those of other borrower types, could be the presence of shared equity mortgages in our data, which we are unable to identify on a transactional basis. These are FTB mortgages that could be reported with lower LTVs because they are being used to buy an agreed share in the property, not the entire property.

Exhibit 15.13: Mortgage performance, by borrower type, any record of past or current missed payments, by LTV band

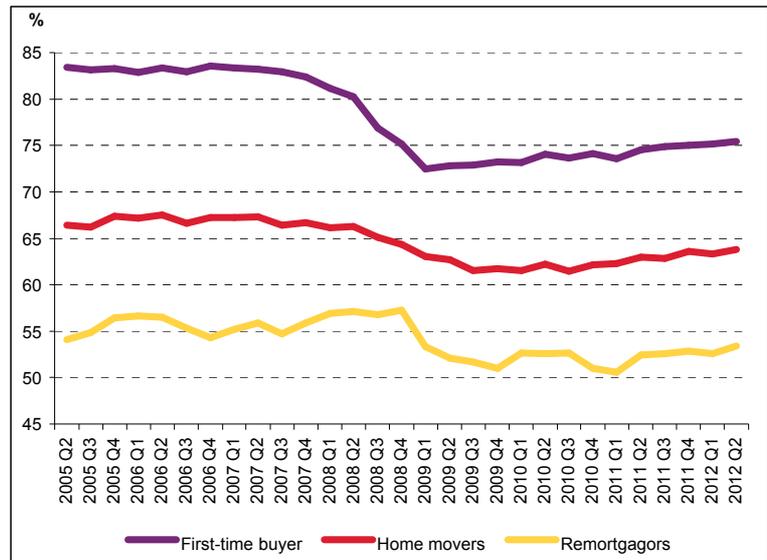


Note: (1) This Exhibit shows performance of mortgages sold in April 2005 – December 2011 that were outstanding as at March 2012 when performance was measured. (2) Performance of RTB borrowers at 95% LTV band is not shown due to a small sample size.

Source: PSD Performance data 2012

- In comparison with other borrower types, FTBs take out higher-LTV mortgages.
- In 2005-2007, the average LTV of FTBs was around 83%, compared with 74% in 2009-2012.
- As shown in Exhibit 4.11, the availability of higher-LTV mortgages has reduced following the tightening of lending criteria since 2008.

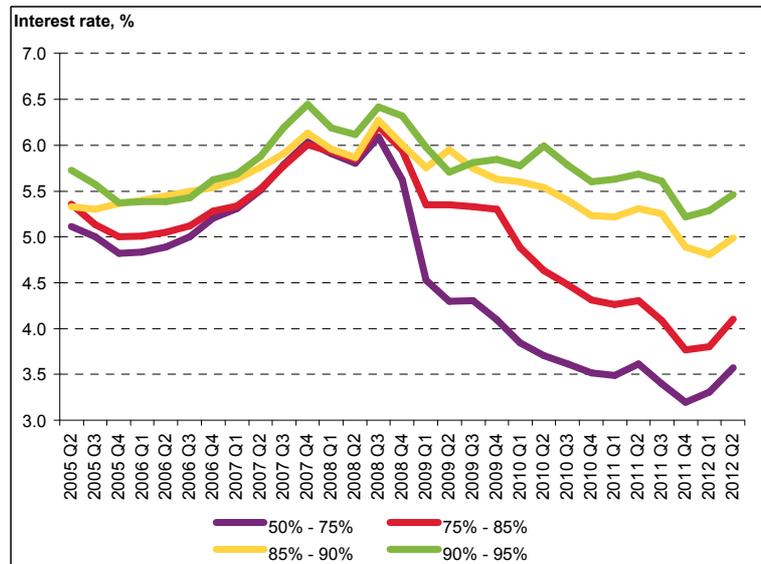
Exhibit 15.14: Average LTV, by borrower type



Source: FSA PSD

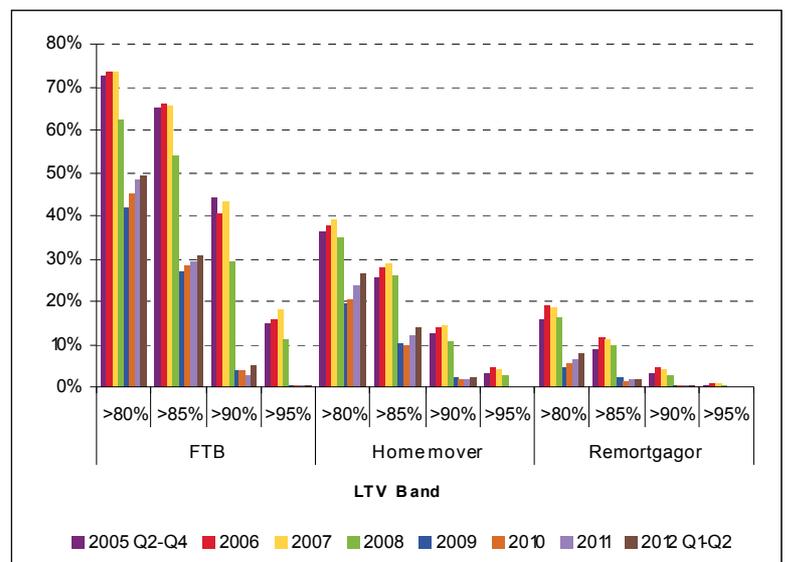
- Higher LTV mortgages are currently considerably more expensive than lower LTV mortgages.
- Higher prices may have reduced demand for higher LTV products amongst FTBs and prompted some to save instead for larger deposits.

Exhibit 15.15: Average initial interest rates on mortgages to FTBs, by LTV band



Source: FSA PSD

- In 2005-2007, over 40% of all mortgages to FTBs had LTVs over 90%. In 2011, this has reduced to only 3%.
- Because of the tightening of lending criteria, we estimate that around 55% of former FTBs who obtained mortgages in 2005-2011 could be 'mortgage prisoners'.¹⁹
- This is mainly because the high LTV products FTBs would require to remortgage or to move house are limited or no longer available.
- We also estimate that over 20% of former FTBs could be in negative equity.

Exhibit 15.16: Higher-LTV sales, by type of borrower

Source: FSA PSD

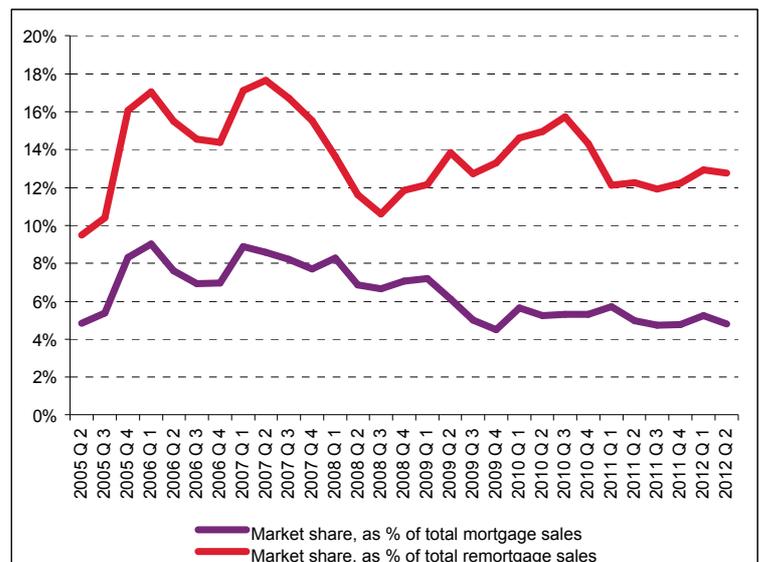
¹⁹ See Chapter 5

16

A closer look at debt consolidation

- At the peak of the market, the proportion of mortgages that involved an element of debt consolidation was significant, accounting for up to 18% of all remortgages and 9% of all mortgage sales.
- These remortgages were used for two purposes – to refinance an existing mortgage and to raise additional money to repay debts, e.g. credit card debts, personal loans or car loans.
- By consolidating unsecured debts in a mortgage, borrowers may have benefited from a lower interest rate, but may have put their homes at risk. Indeed, our data shows that repossessions on mortgages that involved debt consolidation are significantly higher than average (see Exhibit 16.9).
- We do not know how many borrowers who remortgaged for debt consolidation purposes actually repaid their debts from the mortgage.
- Following the market downturn, the size of this market reduced

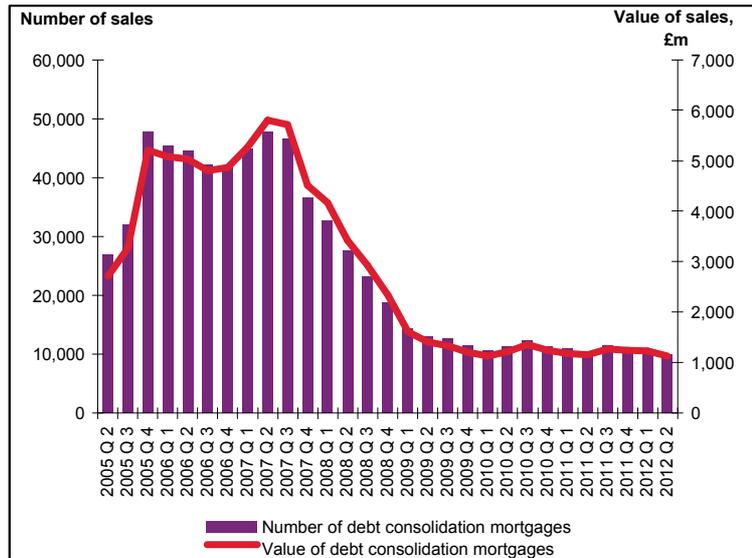
Exhibit 16.1: Market share of debt consolidation mortgages



Source: FSA PSD

considerably in absolute terms. In relative terms, the reduction was less significant.

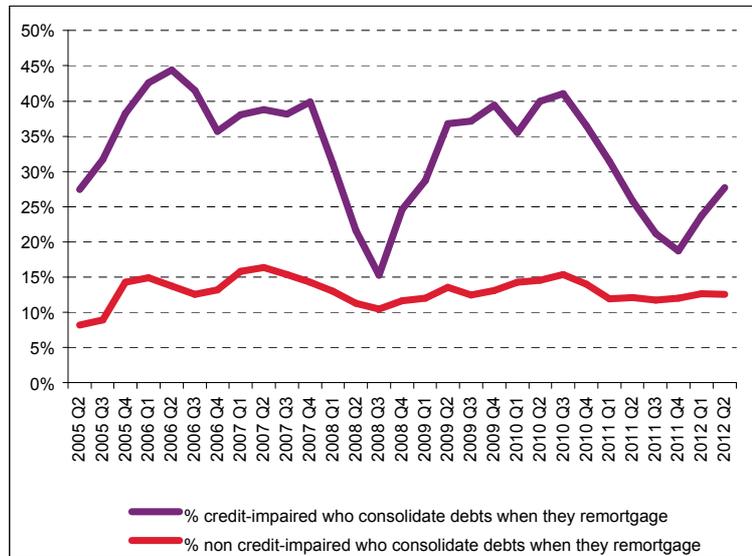
Exhibit 16.2: Number and value of debt consolidation mortgages



Source: FSA PSD

- Borrowers with known past debt problems (credit-impaired) were much more likely than borrowers with a clean credit history to consolidate debts.
- In April 2005 to June 2012, 36% of credit-impaired borrowers took out money for debt consolidation purposes when they remortgaged, in comparison with 13% of borrowers with a clean credit history.

Exhibit 16.3: Remortgage for debt consolidation in total remortgages, by type of credit history



Source: FSA PSD

- At the peak of the market, credit-impaired borrowers accounted for just 4% of all mortgage sales, but for up to one fifth of the debt consolidation market.

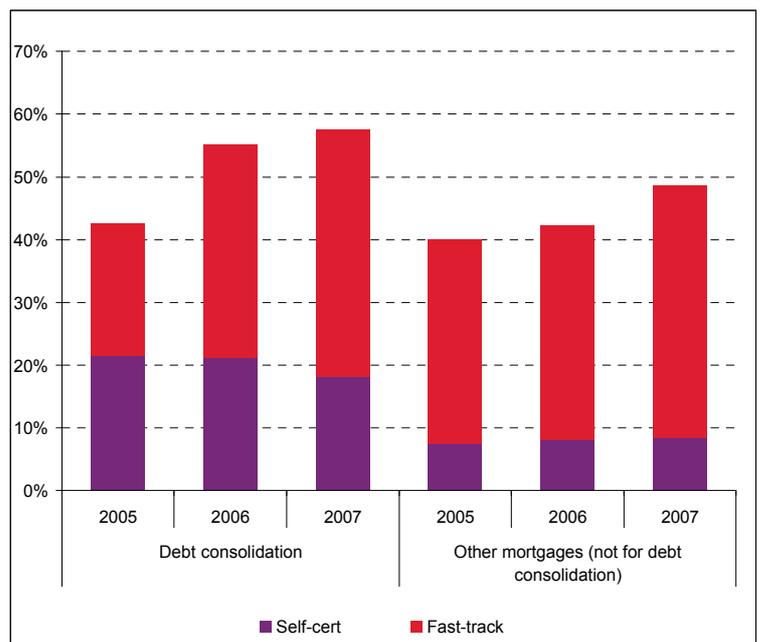
Exhibit 16.4: Share of credit-impaired borrowers in total mortgage sales and in sales for debt consolidation



Source: FSA PSD

- Regardless of a high likelihood of being over-indebted, over half of all borrowers who consolidated debts in the run-up to the crisis did not have their incomes checked. Around 20% were allowed to self-certify their income.
- From 2005 to 2007, the proportion of mortgage sales for debt consolidation purposes where incomes were not verified increased significantly – from just over 40% in 2005 to nearly 60% in 2007.
- Over this period, lenders were less likely to verify the incomes of those who were consolidating debts than of those who were taking out mortgages for other purposes.

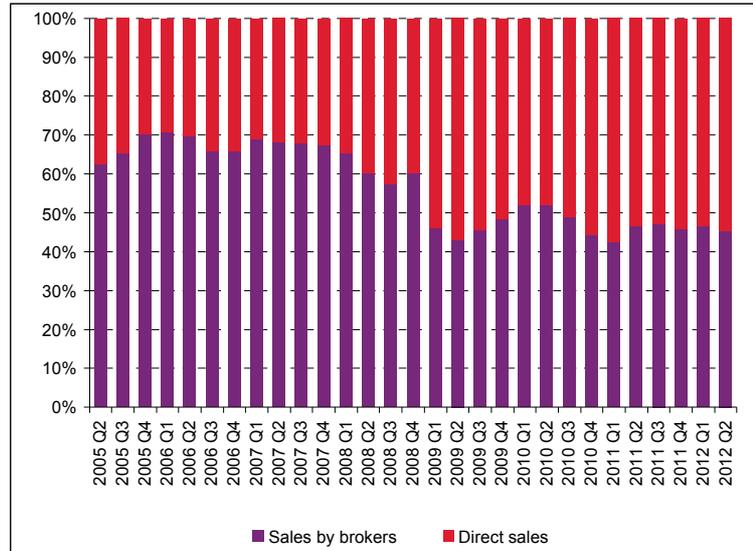
Exhibit 16.5: Proportion of borrowers whose income was not verified in the run-up to the market downturn, by mortgage type



Source: PSD Performance data 2011

- In the run-up to the crisis, the majority of debt consolidation sales were by brokers – up to 70% of the total. The trend has reversed following the market downturn, with over 50% of debt consolidation sales now being made directly by lenders. However, as seen in Exhibit 16.2, the size of this market has considerably reduced.

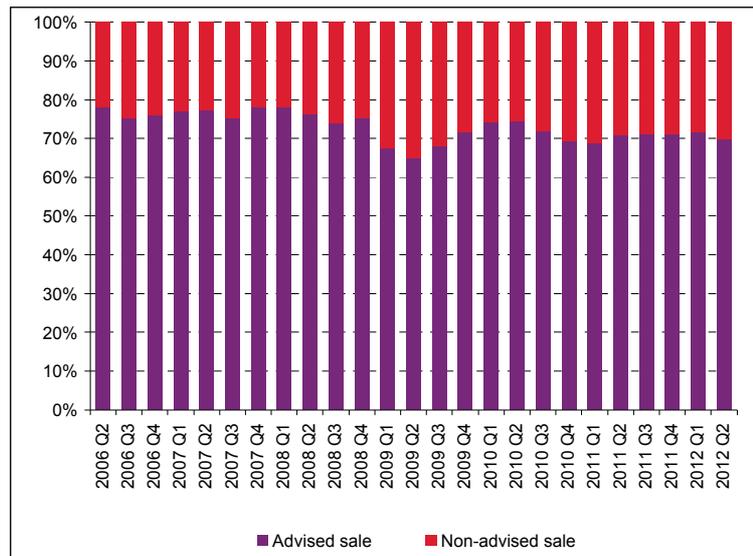
Exhibit 16.6: Debt consolidation mortgages, by channel of sale



Source: FSA PSD

- Most debt consolidation sales are advised. However, up to 30% of consumers did not receive any advice when they consolidated debts.

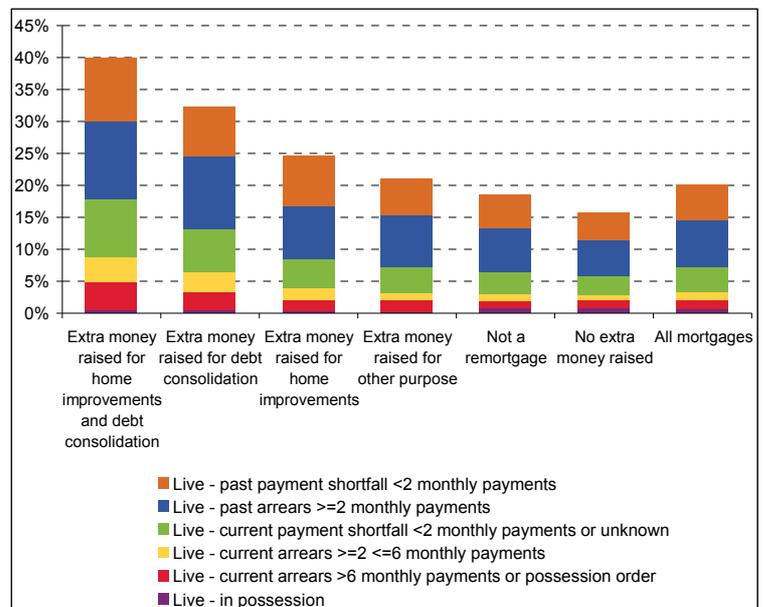
Exhibit 16.7: Proportion of advised and non-advised sales for debt consolidation



Source: FSA PSD

- Unsurprisingly, mortgages that involved debt consolidation (the first two categories in Exhibit 16.8) perform worse than other mortgages.

Exhibit 16.8: Mortgage performance, by type of remortgage

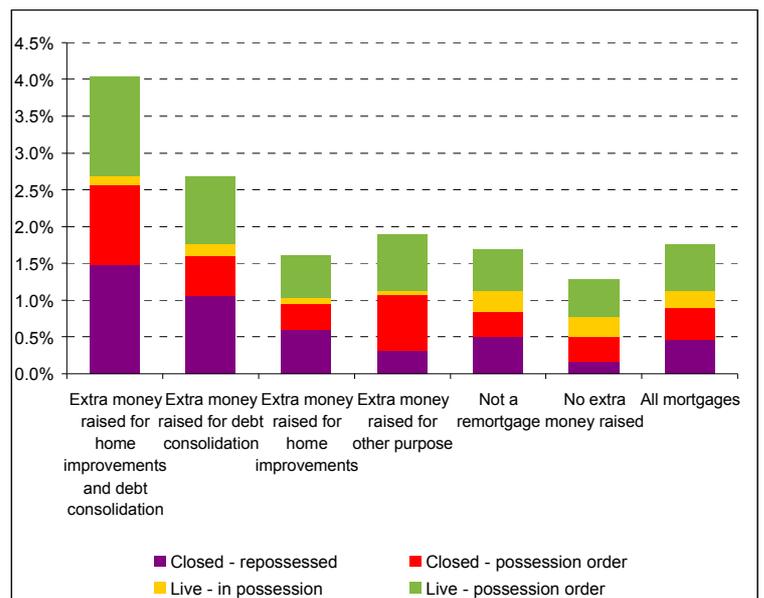


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Borrowers with debt consolidation mortgages were also twice as likely than average to have their home repossessed or to have a possession order made against their property.

Exhibit 16.9: Mortgage repossessions, by type of remortgage



Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Even in the absence of other risk factors, consumers who used mortgages to consolidate debt were nearly three times as likely to be in arrears of two months or more (here, we have compared risk types one and four from our risk combinations matrix).

Exhibit 16.10: Risk combinations and mortgage performance, debt consolidation

Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of sales	Outstanding mortgages			All sales Total: possessions and possession orders
							Total: any record of missed payments	Total: current missed payments or arrears	Total: current arrears 2+ months	
1	NO	NO	NO	NO	NO	53.5%	13.6%	3.3%	1.1%	0.4%
4	NO	NO	NO	YES	NO	3.1%	23.3%	7.4%	3.0%	0.7%
6	NO	YES	NO	YES	NO	1.2%	36.9%	16.1%	8.2%	4.0%
7	NO	NO	YES	YES	NO	0.5%	38.0%	15.3%	7.6%	1.8%
11	NO	YES	YES	YES	NO	0.2%	56.5%	29.7%	16.6%	7.6%
15	YES	NO	NO	YES	NO	0.2%	68.3%	35.9%	17.1%	6.7%
17	YES	YES	NO	YES	NO	0.2%	76.4%	44.5%	24.5%	13.7%
19	YES	NO	YES	YES	NO	0.1%	81.6%	48.8%	26.8%	9.6%
23	YES	YES	YES	YES	NO	0.1%	86.6%	56.4%	33.2%	17.6%
Total						100.0%	20.0%	7.1%	3.4%	1.8%

Note: This is an extract from the full illustration on risk combinations in Exhibit 6.9.

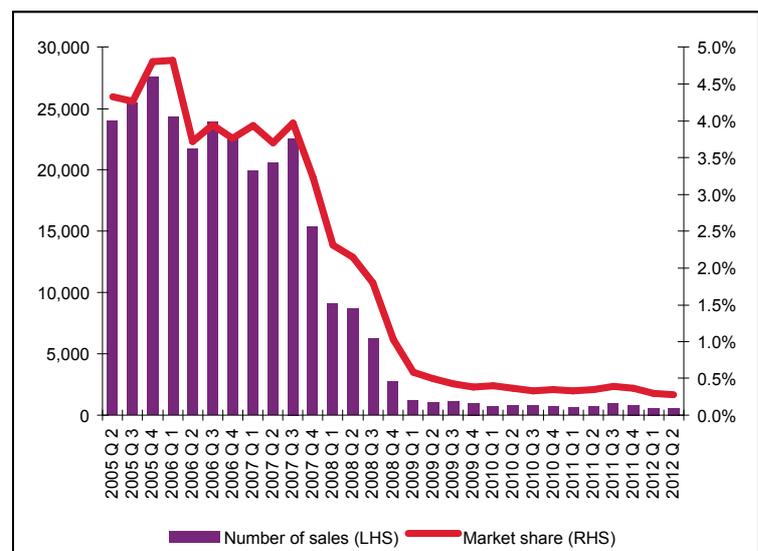
Source: PSD Performance data 2012

17

A closer look at credit-impaired

- As illustrated in Exhibit 4.10, in 2007, up to 8,000 mortgage products were marketed specifically to impaired credit borrowers.
- Although the market share of sales to credit-impaired borrowers was never very large (4.7% of total is the highest quarterly record observed in Q4 2005 to Q1 2006), the number of sales to such borrowers was quite material and stood, for example, at over 90,000 sales in 2006.
- There was a dramatic reduction in sales to the credit-impaired following the downturn and the tightening of lending criteria. In 2011, just over 3,100 sales (under 0.4% of all sales) were to the credit-impaired.

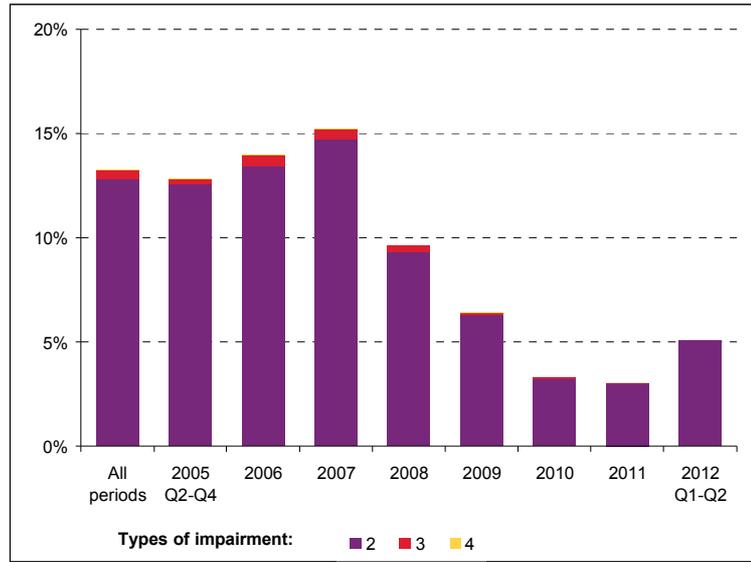
Exhibit 17.1: Mortgage sales to credit-impaired borrowers



Source: FSA PSD

- The majority of credit-impaired borrowers (over 86% in total) have just one type of credit-impairment. This could be arrears, an Individual Voluntary Arrangement (IVA), bankruptcy or County Court Judgement (CCJ).
- However, in the run-up to the crisis, it was not uncommon for a borrower to have many different types of past payment problems when entering a mortgage contract.

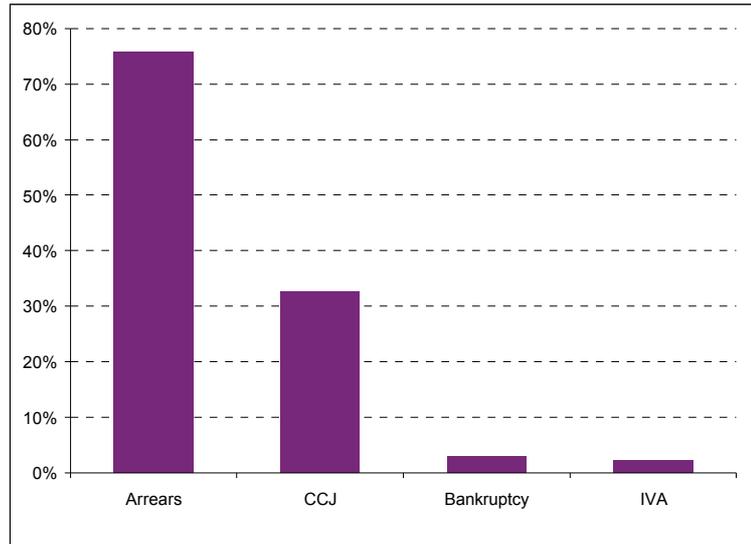
Exhibit 17.2: Proportion of credit-impaired borrowers with two or more types of impairment



Source: FSA PSD

- Past arrears is the most common type of credit impairment – 76% of credit-impaired borrowers have them. This is followed by county court judgments (CCJs), where debts have been recorded through the courts (33%).

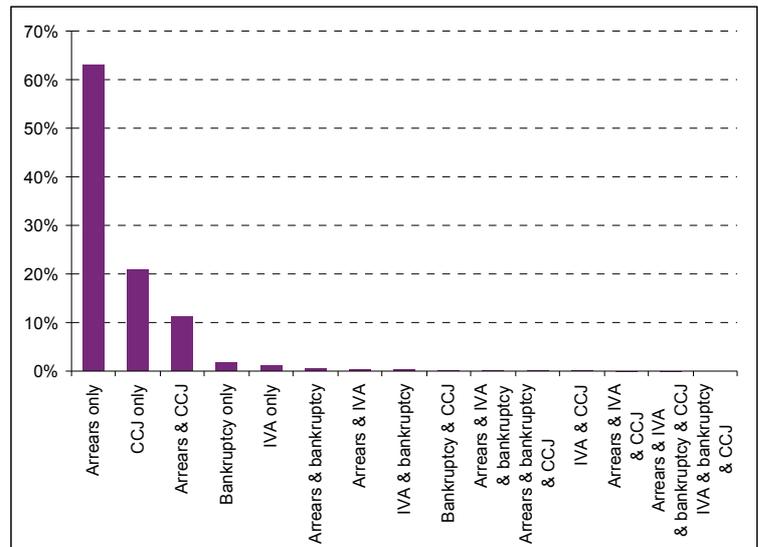
Exhibit 17.3: Credit impairments by type, April 2005 to June 2012 (part 1)



Source: FSA PSD

- Among borrowers with several types of impairment, a combination of arrears and CCJs is the most common – overall, about 11% of credit-impaired borrowers have this combination.

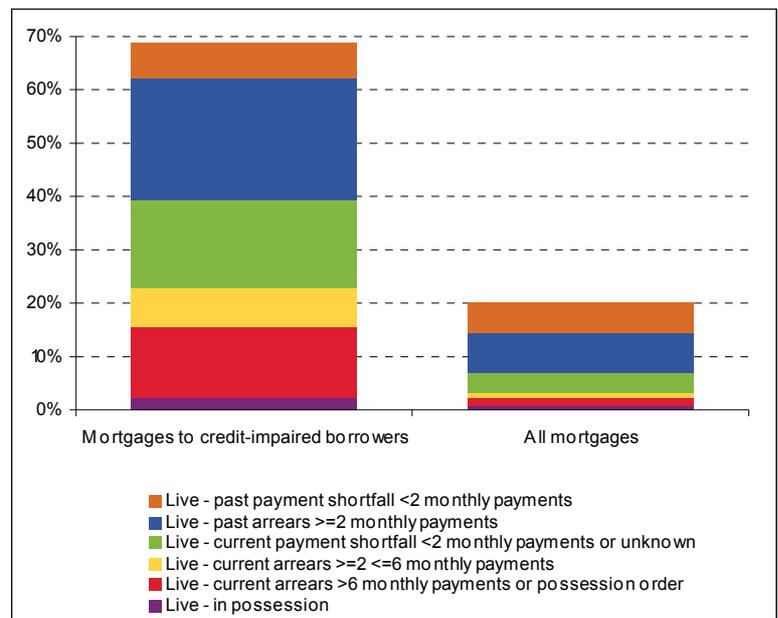
Exhibit 17.4: Credit impairments by type, April 2005 to June 2012 (part 2)



Source: FSA PSD

- Credit-impaired mortgages perform considerably worse than other mortgages: 69% of credit-impaired mortgages have a record of current or past payment problems.

Exhibit 17.5: Mortgage performance, by type of credit history

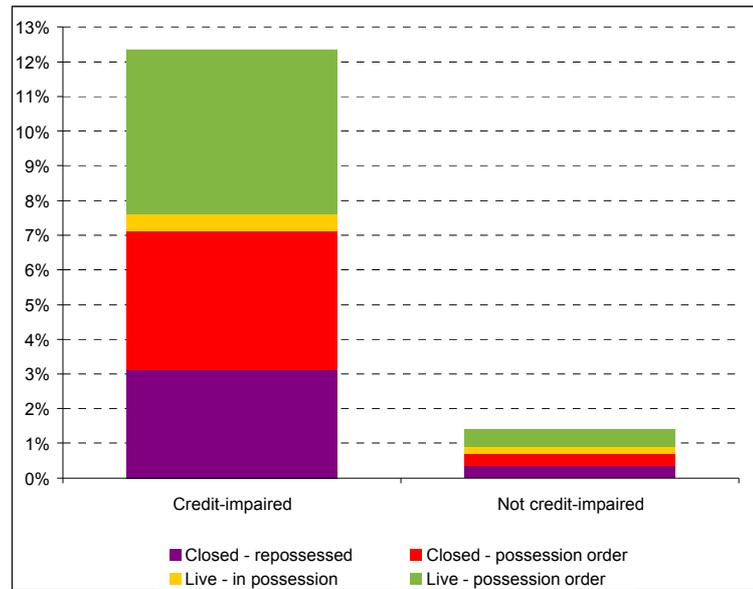


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- For over 12% of credit-impaired borrowers (or one in 8), payment problems have ended in their homes being repossessed or a possession order being made. These figures are likely to increase as credit-impaired mortgages mature.

Exhibit 17.6: Mortgage repossessions, by type of credit history



Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Even in the absence of other risk factors, credit-impaired borrowers are nearly 16 times more likely to be in arrears of two months or more and nearly 20 times more likely to have their homes repossessed (here, we have compared risk types one and 12 from our risk combinations matrix).

Exhibit 17.7: Risk combinations and mortgage performance, credit-impaired

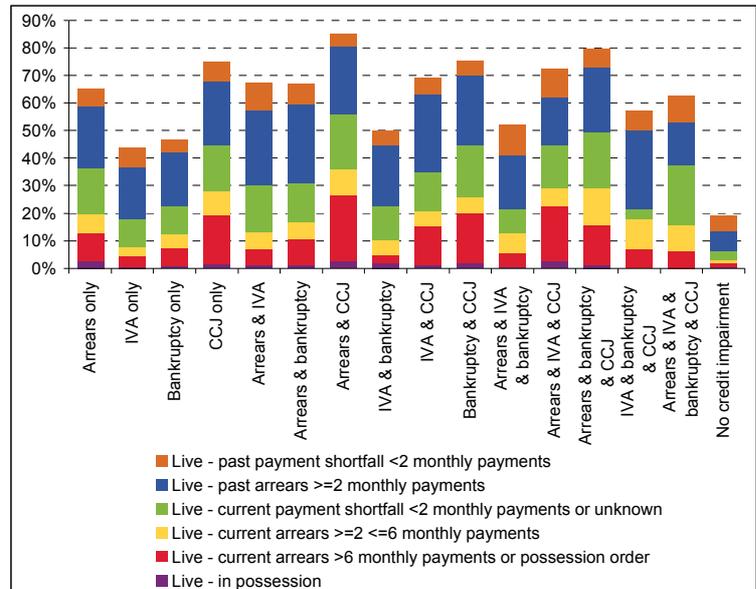
Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of sales	Outstanding mortgages			All sales Total: possession and possession orders
							Total: any record of missed payments	Total: current missed payments or arrears	Total: current arrears 2+ months	
1	NO	NO	NO	NO	NO	53.5%	13.6%	3.3%	1.1%	0.4%
12	YES	NO	NO	NO	NO	1.0%	60.8%	31.8%	17.2%	7.9%
14	YES	YES	NO	NO	NO	0.8%	67.1%	39.7%	24.9%	15.3%
15	YES	NO	NO	YES	NO	0.2%	68.3%	35.9%	17.1%	6.7%
16	YES	NO	YES	NO	NO	0.4%	75.3%	44.4%	26.0%	12.0%
17	YES	YES	NO	YES	NO	0.2%	76.4%	44.5%	24.5%	13.7%
18	YES	NO	NO	NO	YES	0.1%	79.1%	39.4%	21.8%	13.0%
19	YES	NO	YES	YES	NO	0.1%	81.6%	48.8%	26.8%	9.6%
20	YES	YES	YES	NO	NO	0.3%	81.9%	53.7%	34.6%	21.3%
21	YES	YES	NO	NO	YES	0.0%	82.8%	46.9%	26.2%	21.1%
22	YES	YES	YES	NO	YES	0.0%	85.0%	50.4%	32.5%	26.6%
23	YES	YES	YES	YES	NO	0.1%	86.6%	56.4%	33.2%	17.6%
24	YES	NO	YES	NO	YES	0.0%	88.6%	49.5%	23.8%	13.7%
Total						100.0%	20.0%	7.1%	3.4%	1.8%

Note: This is an extract from the full illustration on risk combinations in Exhibit 6.9.

Source: PSD Performance data 2012

- Among the different types of credit-impairment, borrowers with CCJs generally perform the worst.
- Amongst borrowers with a record of arrears and CCJs, over 85% have developed payment problems on their current mortgage.

Exhibit 17.8: Mortgage performance, by type of credit impairment

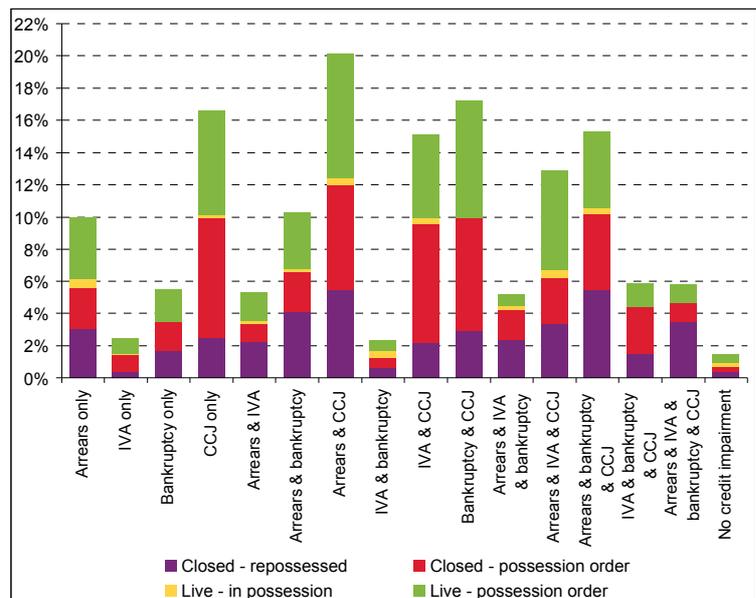


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- A similar trend is observed in repossessions – for example, of all sales to borrowers with a record of arrears and CCJs made between April 2005 and December 2011, 20% have had their homes repossessed or had a possession order made.

Exhibit 17.9: Mortgage repossessions, by type of credit impairment



Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

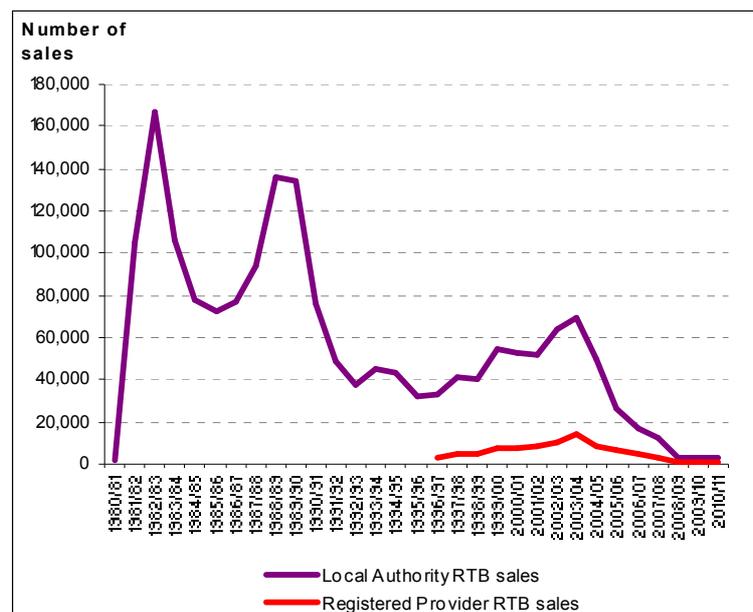
Source: PSD Performance data 2012

18

A closer look at right-to-buy mortgages

- Many households in the UK have bought their homes through a Right-to-Buy (RTB) scheme.
- There was great interest in RTB sales in the first few years after the scheme was launched - but this has now considerably reduced.
- There were only 3,690 homes sold through a RTB scheme in the financial year 2010/11 according to Communities and Local Government (DCLG).
- However, the government recently announced, in its new Housing Strategy²⁰, its intention to increase the RTB discount with the intention of stimulating demand.

Exhibit 18.1: Right-to-buy sales in England – time trend, 1980-2011

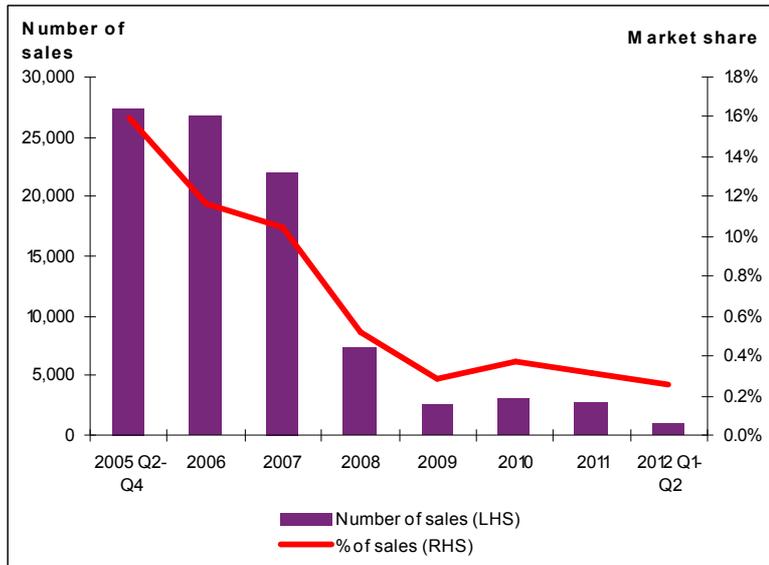


Source: DCLG

²⁰ For more information on the Housing Strategy see www.communities.gov.uk/news/corporate/2033724

- The RTB mortgage market is relatively small. In 2011, there were 2,722 RTB mortgages which accounted for just 0.3% of all mortgage sales – a reduction from 1.6% in 2005.

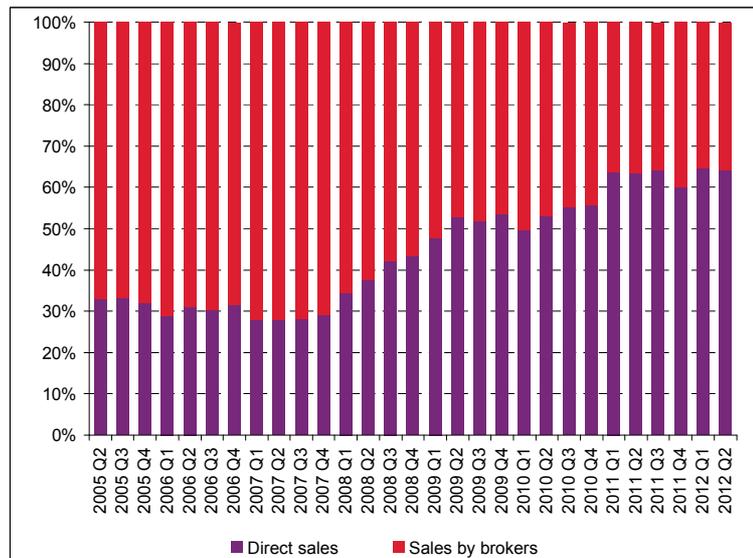
Exhibit 18.2: Number and market share of RTB mortgage sales



Source: FSA PSD

- While in 2005-2008 the majority of RTB sales were by brokers, in early 2009 the trend reversed and currently the majority of RTB mortgages are sold directly by lenders.
- This could be a simple reflection of the fact that the current size of the RTB mortgage market is very small.

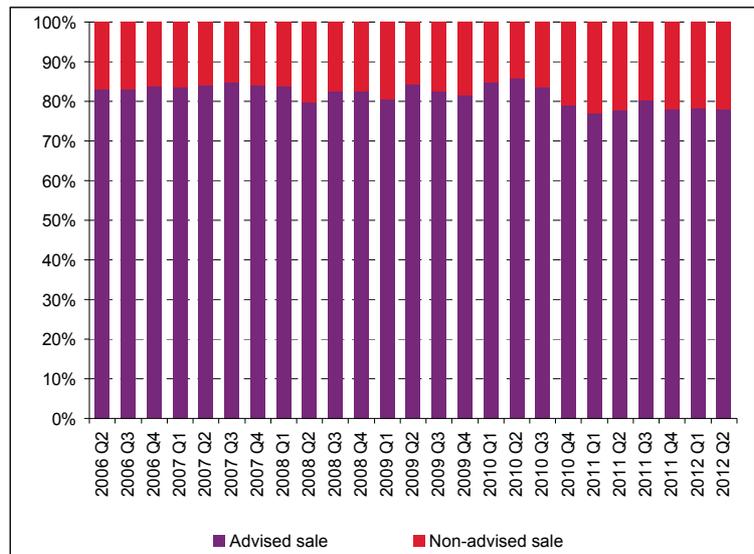
Exhibit 18.3: Proportion of RTB sales, by channels



Source: FSA PSD

- Most RTB mortgages are sold with advice.

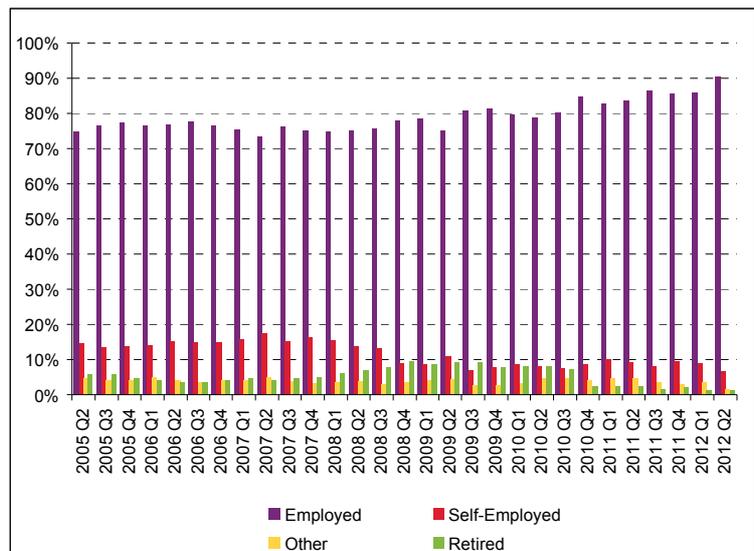
Exhibit 18.4: Proportion of advised and non-advised right-to-buy sales



Source: FSA PSD

- The majority of RTB borrowers are in employment and this has been a stable trend from Q2 2005 to the present.
- In 2011, 85% of people who bought RTB properties with a mortgage were employed, while only 9% were self-employed.

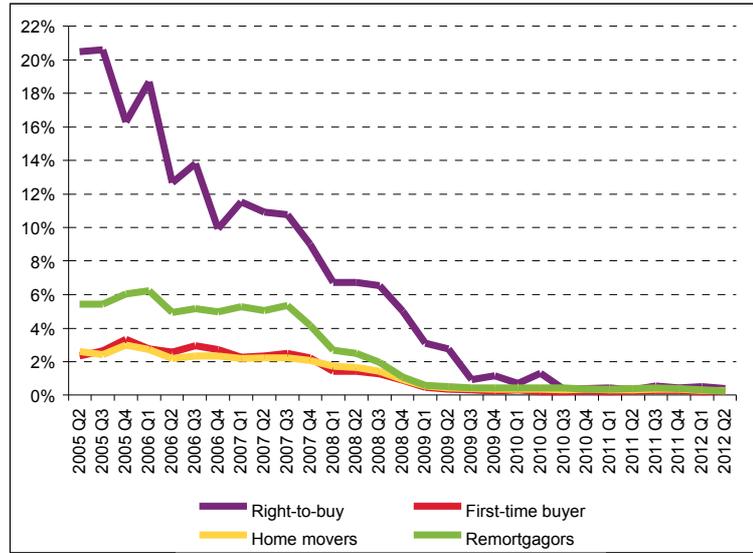
Exhibit 18.5: Right-to-buy, % of sales, by employment status



Source: FSA PSD

- Following the tightening of lending criteria by lenders, the quality of the RTB mortgage sales has significantly improved.
- Historically, RTB borrowers were much more likely than other borrower types to be credit-impaired. However, this was no longer observed in 2010-2012 lending. Only 0.4% of RTB borrowers were credit-impaired in Q2 2012, compared to 21% in Q3 2005.

Exhibit 18.6: Proportion of credit-impaired, by borrower type



Source: FSA PSD

- A similar trend was observed in interest-only sales to RTB borrowers. In 2007, up to 30% of sales to RTB borrowers were on an interest-only basis – by Q2 2012, this had reduced to just 2%

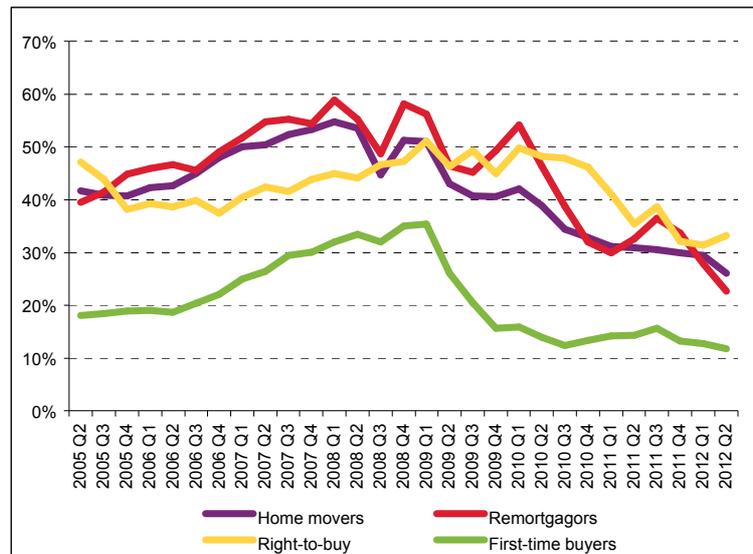
Exhibit 18.7: Interest-only mortgage sales, by borrower type



Source: FSA PSD

- However, even in Q2 2012, lenders were not verifying incomes of 33% of RTB borrowers (although this was a reduction from previous levels).
- This is likely to be because RTB borrowers, on average, have relatively low LTVs as they are buying their homes at a discounted price which is below market value. It might be therefore that some lenders do not verify the income of RTB borrowers because they do not think that their security is at risk.

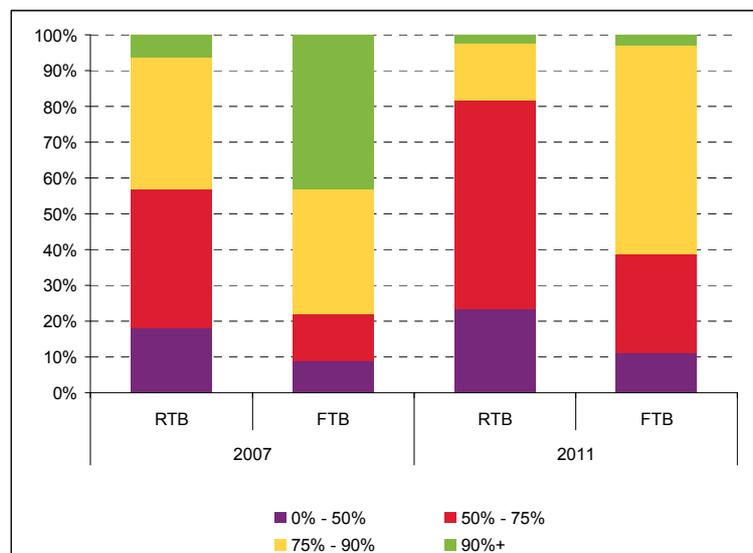
Exhibit 18.8: Mortgage sales where income was not verified, by borrower type



Source: FSA PSD

- To illustrate this, we compare LTVs of RTB and FTB borrowers. In 2011, 82% of RTB borrowed at LTVs below 75% compared to only 39% of FTBs. A similar difference was observed in 2007.
- The fact that some RTB mortgages are at higher LTVs may indicate over-borrowing, i.e. where a part of the mortgage is being used for needs other than house purchase (e.g. consumption or debt consolidation).

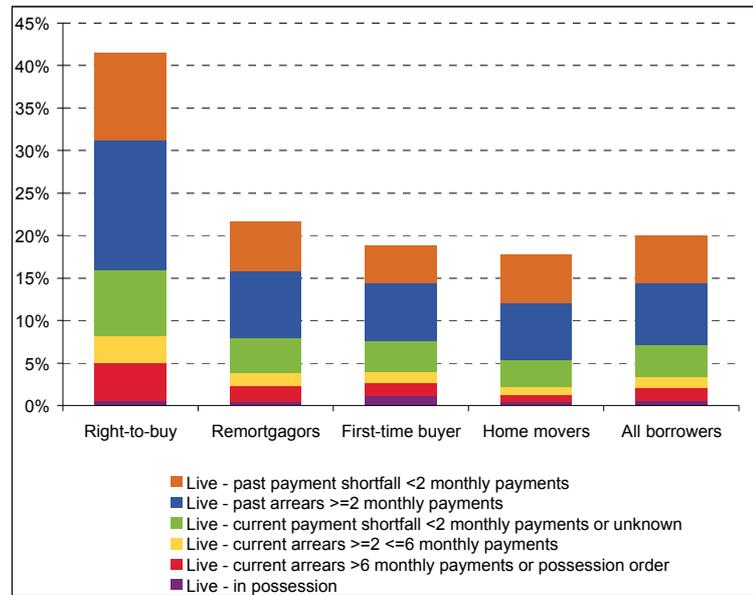
Exhibit 18.9: Mortgage sales to FTB and RTB, by LTV band



Source: FSA PSD

- Of all borrower types, RTB borrowers are the most likely to experience arrears and payment problems. 41% of current RTB borrowers have a record of payment problems of some kind, with 8% being in current arrears of two months or more.

Exhibit 18.10: Mortgage performance, by type of borrower

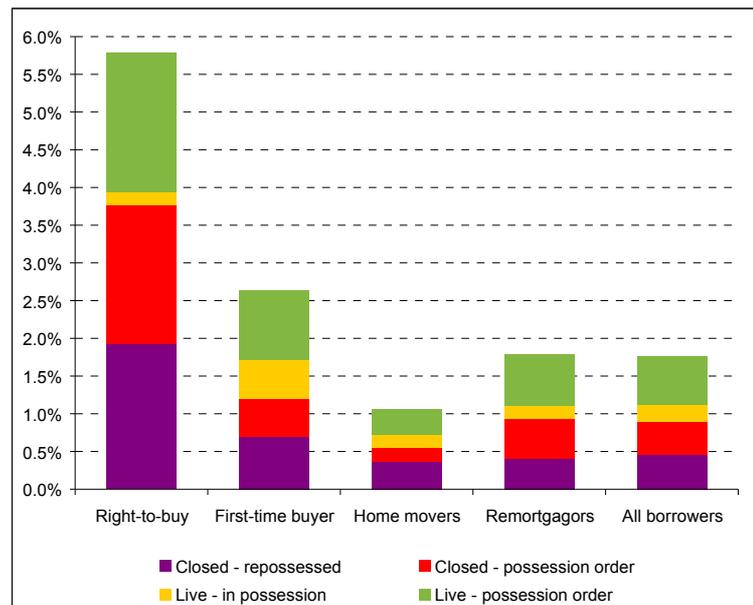


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- RTB borrowers are also more likely than other types of borrowers to have their homes repossessed. Around one in 17 RTB borrowers have had their homes repossessed or a possession order made.

Exhibit 18.11: Mortgage repossessions, by type of borrower



Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- Even in the absence of other risk factors, RTB borrowers are four times more likely than other borrower types to be in arrears of two months or more and six times more likely to have their property repossessed (here, we have compared risk types one and five from our risk combinations matrix).
- Given the recent improvements in the risk profile of RTB sales (e.g. the proportional reduction of sale to credit-impaired), it is likely that arrears and repossessions on RTB mortgages sold in 2009-2010 will be lower than those observed historically²¹.

Exhibit 18.12: Risk combinations and mortgage performance - RTB

Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	% of sales	Outstanding mortgages			All sales Total: possessions and possession orders
							Total: any record of missed payments	Total: current missed payments or arrears	Total: current arrears 2+ months	
1	NO	NO	NO	NO	NO	53.5%	13.6%	3.3%	1.1%	0.4%
5	NO	NO	NO	NO	YES	0.6%	33.8%	10.1%	4.6%	2.4%
9	NO	YES	NO	NO	YES	0.2%	44.3%	20.5%	11.3%	8.3%
10	NO	NO	YES	NO	YES	0.1%	44.7%	16.9%	8.6%	4.7%
13	NO	YES	YES	NO	YES	0.0%	61.0%	29.7%	18.5%	12.1%
18	YES	NO	NO	NO	YES	0.1%	79.1%	39.4%	21.8%	13.0%
21	YES	YES	NO	NO	YES	0.0%	82.8%	46.9%	26.2%	21.1%
22	YES	YES	YES	NO	YES	0.0%	85.0%	50.4%	32.5%	26.6%
24	YES	NO	YES	NO	YES	0.0%	88.6%	49.5%	23.8%	13.7%
Total						100.0%	20.0%	7.1%	3.4%	1.8%

Note: This is an extract from the full illustration on risk combinations in Exhibit 6.9.

Source: PSD Performance data 2012

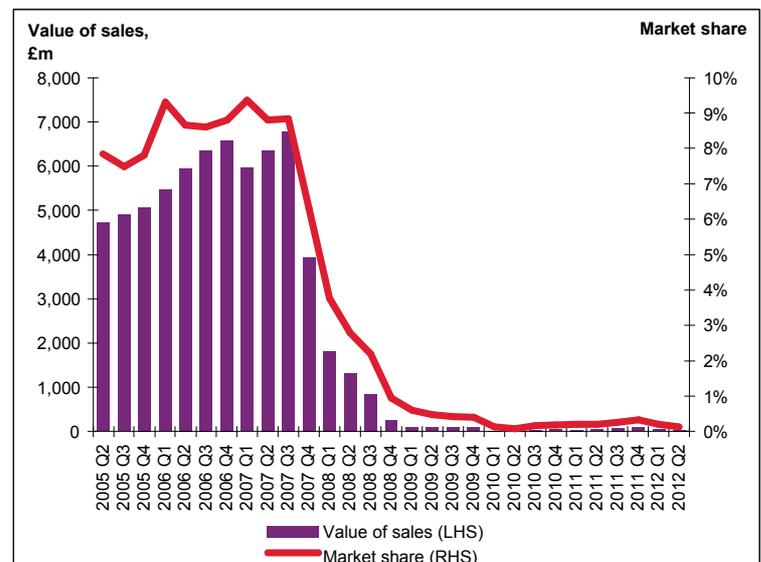
²¹ See Exhibit 6.14 that illustrates a relationship between lending risk and expected arrears.

19

A closer look at specialist lenders

- There are three types of specialist lenders in the mortgages market: standalone specialist lenders (non-deposit taking lenders or ‘non-banks’), subsidiaries of banks and subsidiaries of building societies.
- By 2007, non-banks, some of which were subsidiaries of overseas investment banks, had accumulated a considerable market share and accounted for up to 9% of all regulated mortgage sales.
- As these lenders relied on wholesale funding, when this dried up, most of them exited the market.
- In the run-up to the crisis, many high street lenders (e.g. some building societies) entered the specialist market as well, but often through subsidiary companies, specifically set-up to engage in higher-risk lending practices.

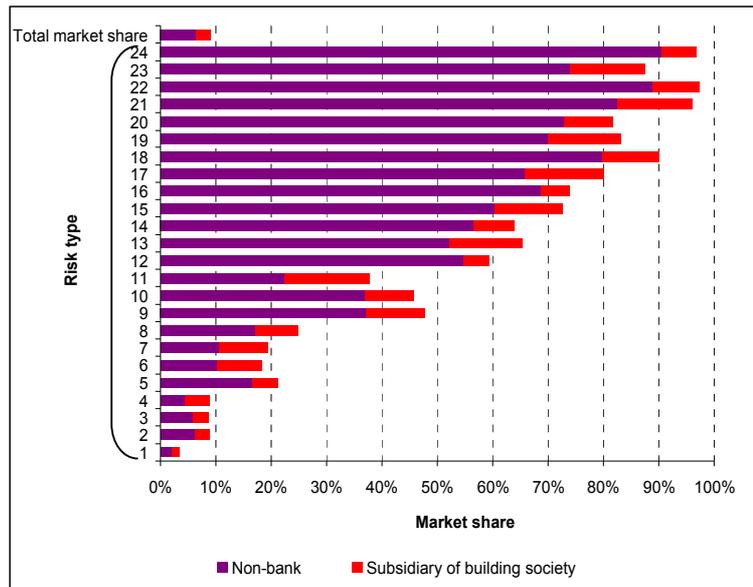
Exhibit 19.1: Regulated mortgage sales by non-banks



Source: FSA PSD, FSA calculation

- Many specialist lenders serviced borrowers who would have found it difficult to obtain mortgages from high-street lenders.
- Nearly all of the highest-risk mortgages were originated by specialist lenders. Here, for illustration purposes, we show the market share of non-banks and subsidiaries of building societies, by type of risk.

Exhibit 19.2: Non-banks and subsidiaries of building societies: market share by risk type (mortgage sales in April 2005 - December 2011)

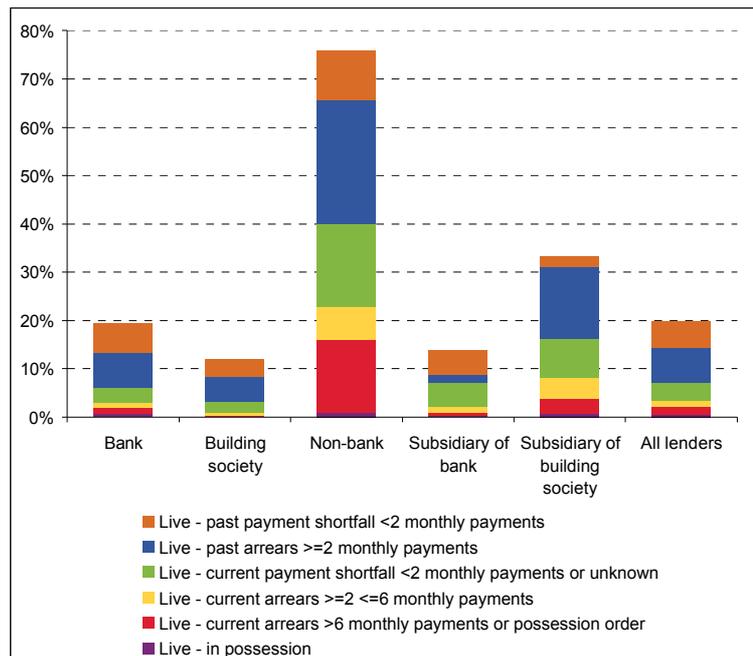


Note: see Exhibit 6.9 for the definitions of risk types

Source: PSD Performance data 2012

- Specialist lenders left many borrowers in serious financial distress.

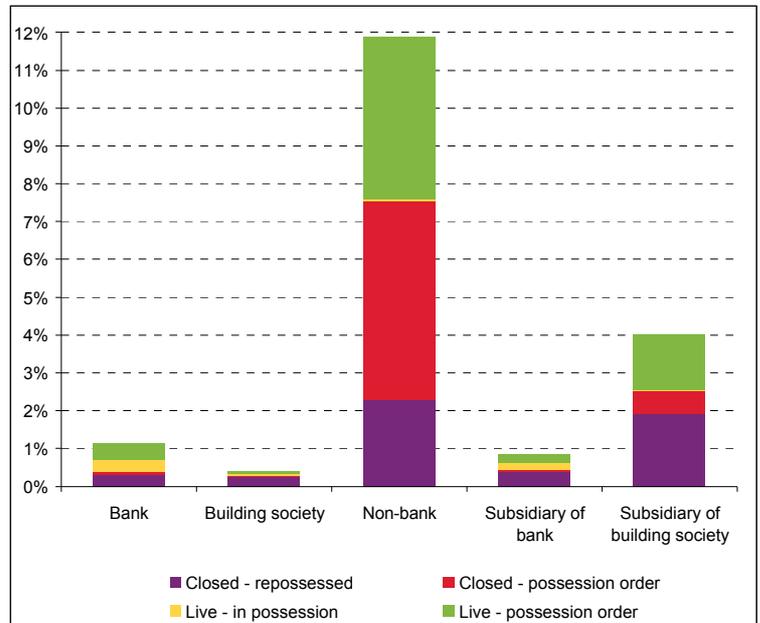
Exhibit 19.3: Mortgage performance, by type of lender



Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

Exhibit 19.4: Mortgage repossessions, by type of lender

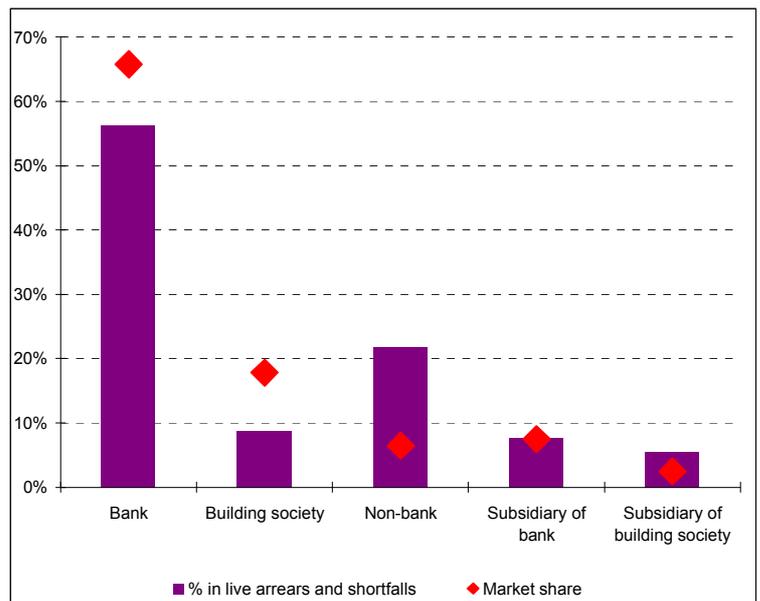


Note: This Exhibit shows repossessions and possession orders on mortgages sold in April 2005 - December 2011 as at March 2012 when performance was measured.

Source: PSD Performance data 2012

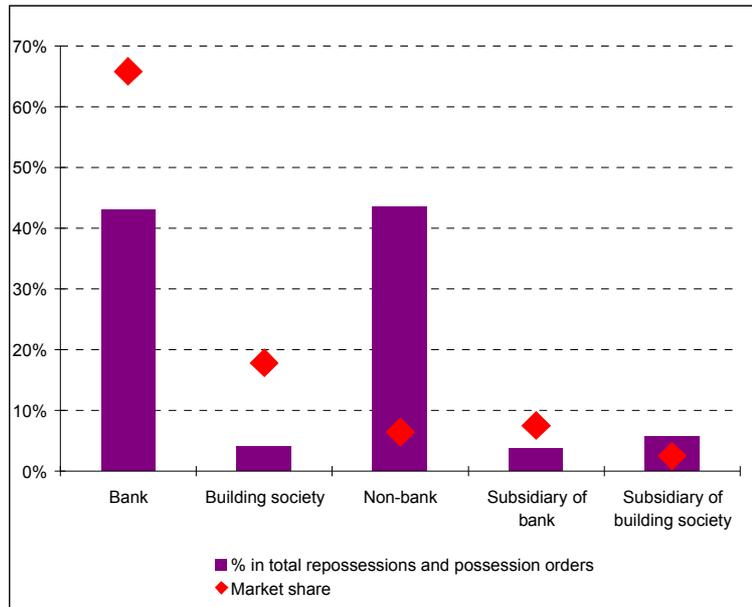
- Overall, specialist lenders account for a much higher proportion of arrears and repossessions than their market share would suggest.
- Over 20% of all arrears and around 44% of all repossessions were accounted for by non-banks.

Exhibit 19.5: Market share and share of live arrears and shortfalls, by type of lender



Source: PSD Performance data 2012

Exhibit 19.6: Market share and share of total possessions and possession orders, by type of lender



Source: PSD Performance data 2012

PART IV

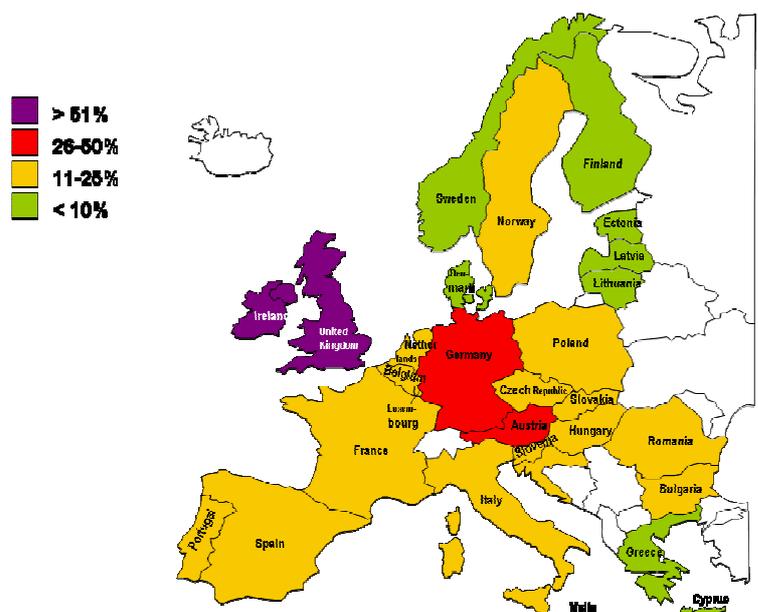
Distribution

20

Channel of sale and advice

- Mortgage brokers play a vital role in the UK mortgage market.
- Their market share is much higher than in any other European country.

Exhibit 20.1: Brokers' share in the EU mortgage market, 2007, % of sales



Source: European Commission (2009), Study on Credit Intermediaries in the Internal Market

- Over a relatively short period of time, the share of brokers in the UK grew considerably.
- In 2005-2008, brokers were responsible for a larger proportion of mortgage business measured by the value of sales than by the number of sales. This is because the mortgages sold by brokers were, on average, larger than the mortgages sold directly by providers.
- This is no longer observed following the tightening of affordability standards by lenders.

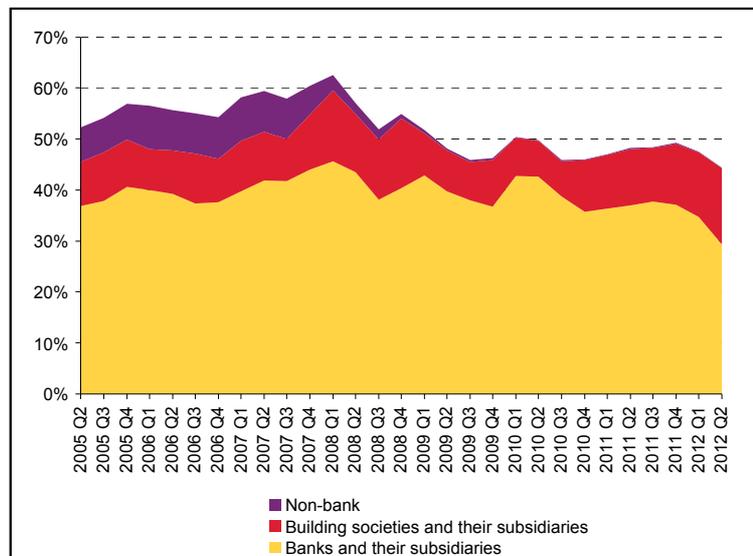
Exhibit 20.2: Share of mortgage sales by brokers



Source: Mintel (2000), FSA PSD (2005-2012)

- To some extent, the market share of brokers was fuelled by the emergence of non-banks who, in the absence of a branch network, relied entirely on this channel.
- The recent reduction in brokers' market share is mainly a result of specialist lenders leaving the market.

Exhibit 20.3: Market share of brokers - types of lenders they were selling for

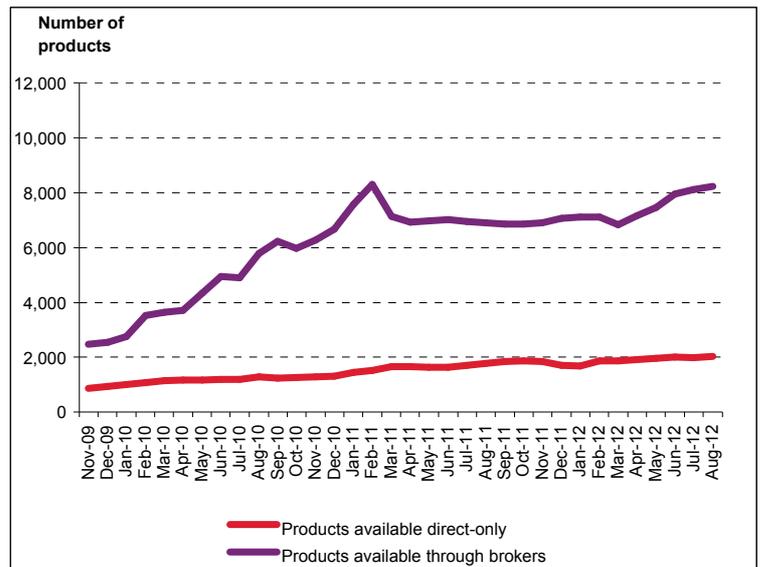


Note: The market share is by number of sales.

Source: FSA PSD

- At the height of the market, there were many thousands of different mortgage products offered, many of which were almost exclusively available through brokers.
- The number of products has reduced significantly since the crisis, although this is now rising again.

Exhibit 20.4: Number of products available direct and through brokers

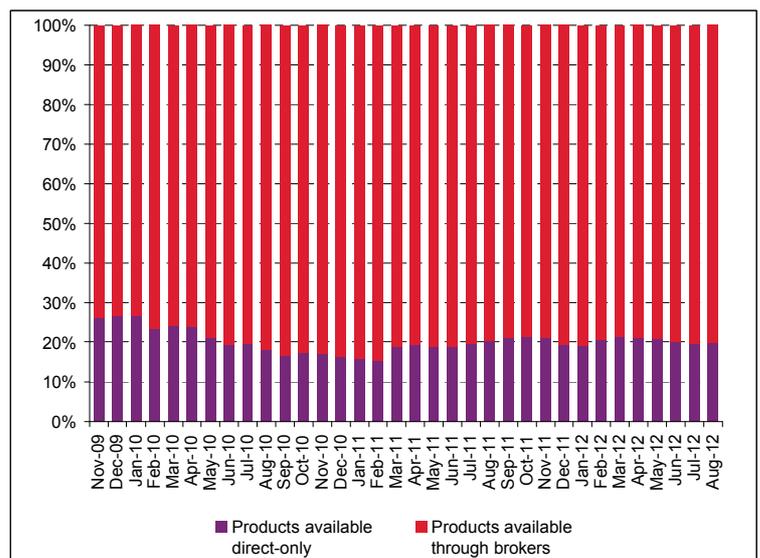


Note: Product numbers have been adjusted for period 4/04/011 to 7/02/2012 due to lenders introducing restricted distribution in the second half of 2011.

Source: Mortgage Brain

- In relative terms, the proportion of products that are only available direct from a lender has reduced – from 26% in November 2009 to 20% in August 2012.
- However, direct-only deals still make up a significant proportion of available products.

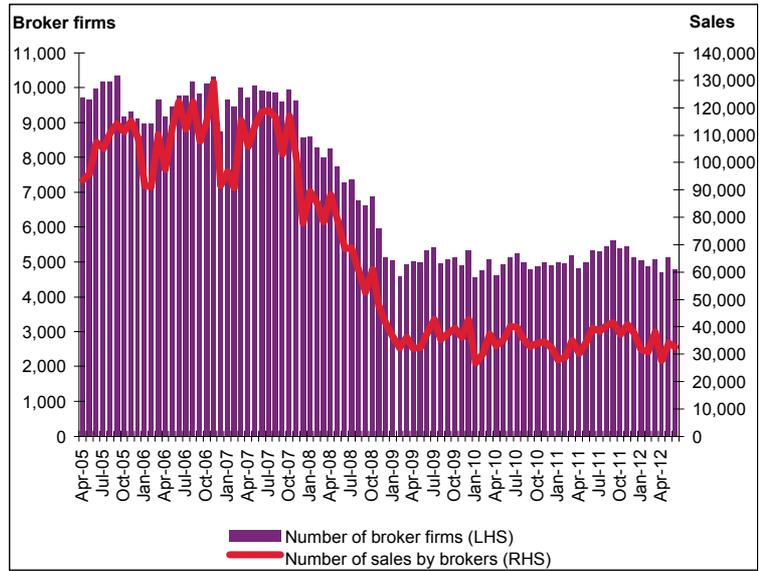
Exhibit 20.5: Proportion of products available direct and through brokers



Source: Mortgage Brain

- The rapid contraction in lending has resulted in the number of broker firms steadily declining.
- Unsurprisingly, the decline in broker firms has coincided with a decline in the number of broker sales, but their overall market share shows considerable resilience.

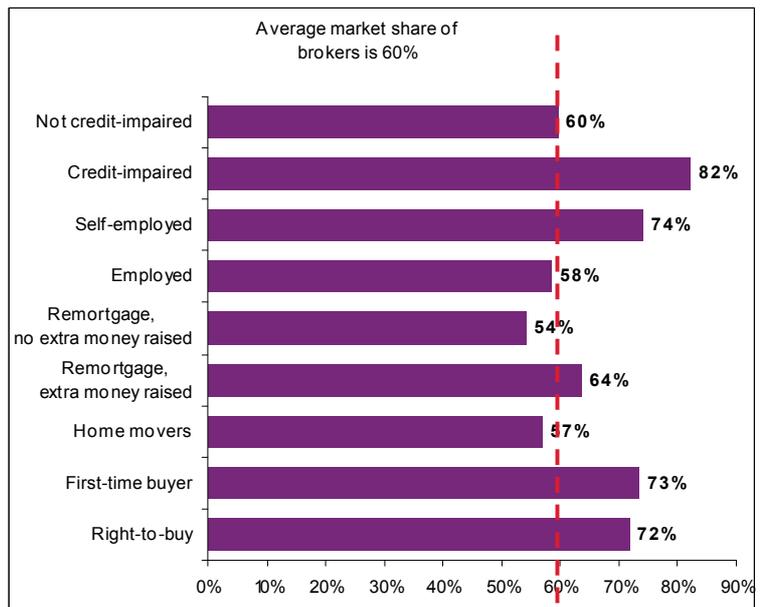
Exhibit 20.6: Number of broker firms and regulated mortgage sales



Source: FSA PSD

- This relatively even split in business belies considerable differences in the customer base.
- Many lenders' sales will be retention deals offered to existing borrowers. Brokers, on the other hand, will help many consumers meet more specialist borrowing needs. So, for example, a much higher population of credit-impaired sales went through brokers (around 80% in 2007).

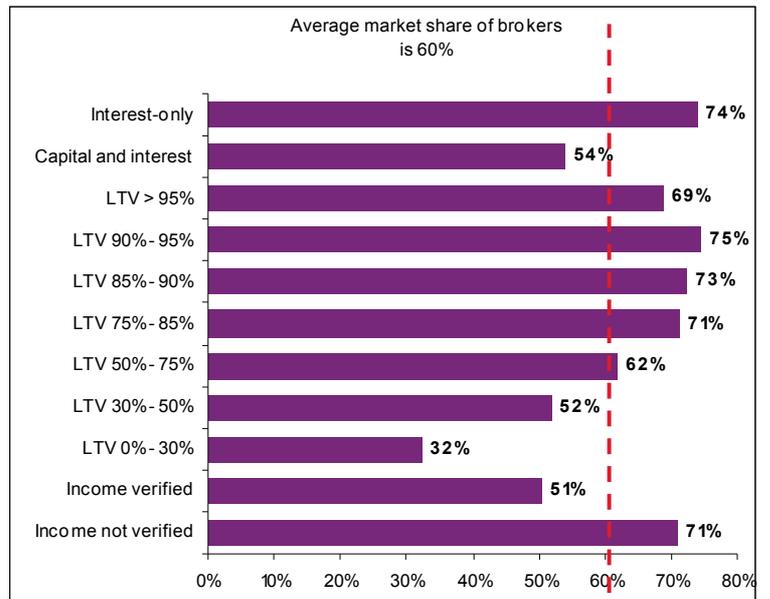
Exhibit 20.7: Share of brokers in total sales, by borrower type, 2007



Source: PSD FSA

- More generally across all products, brokers facilitated a greater proportion of higher-risk business than lenders directly.

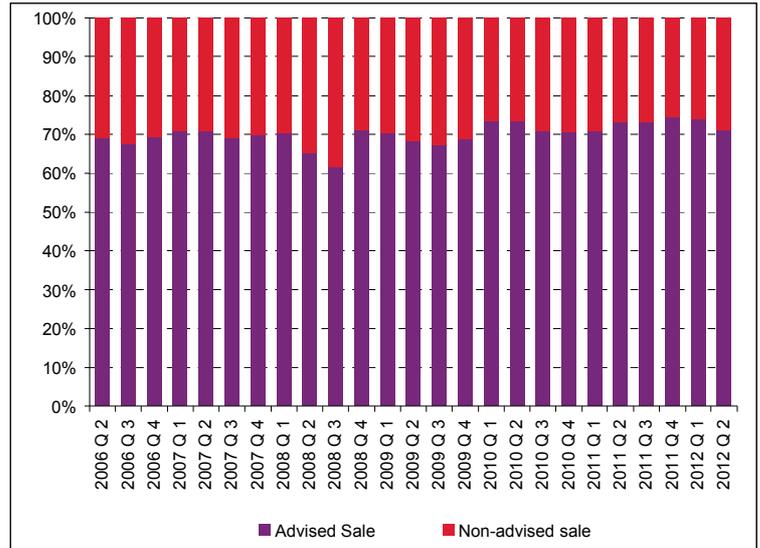
Exhibit 20.8: Share of brokers in total sales, by product, 2007



Source: FSA PSD

- Out of all mortgage sales most – around 70% – are sold with advice.

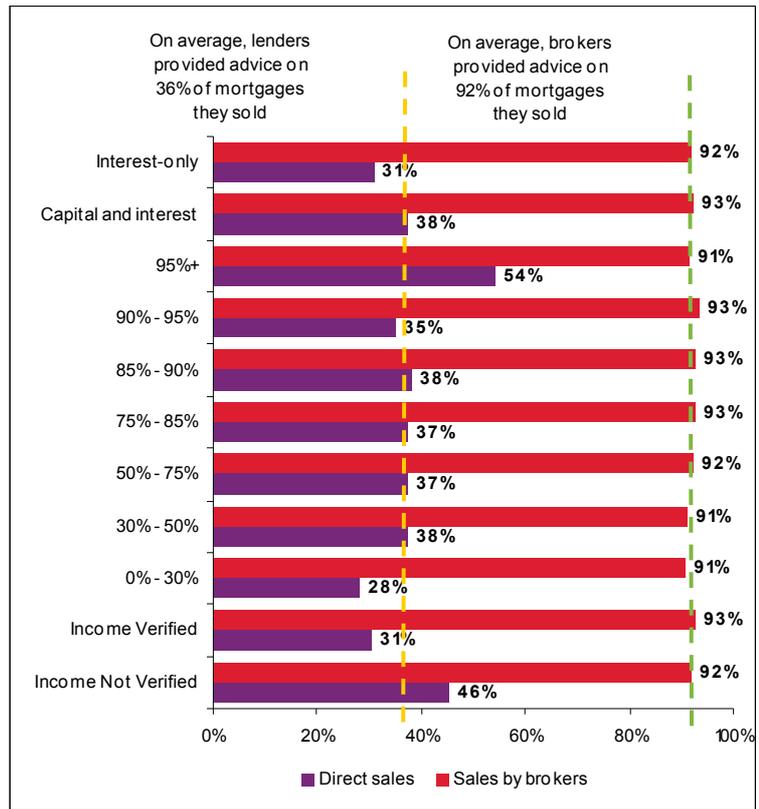
Exhibit 20.9: Proportion of advised and non-advised mortgage sales



Source: FSA PSD

- One reason a consumer may use a broker is that they provide advice in the vast majority of their sales, regardless of the borrower’s or product’s risk characteristics.

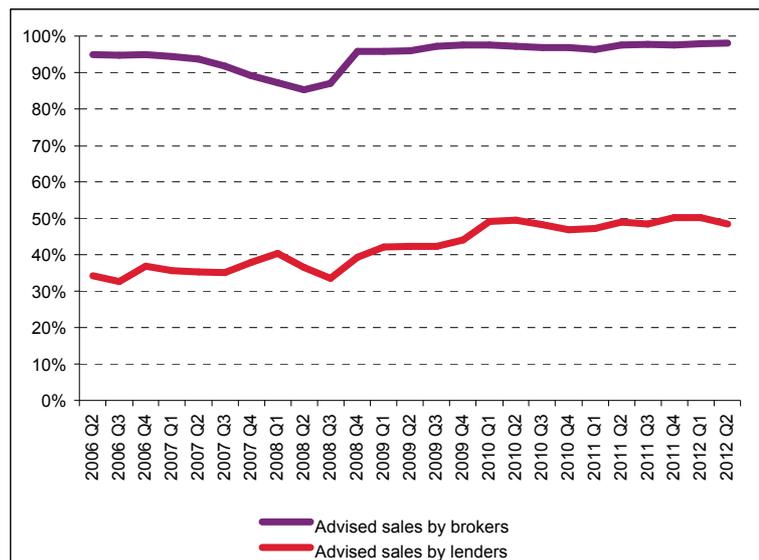
Exhibit 20.10: Proportion of mortgages sold with advice, by channel and product type, 2007



Source: PSD FSA

- On average less than half of all direct sales are advised, although this has been steadily increasing – from 34% in Q2 2006 to 49% in Q2 2012.

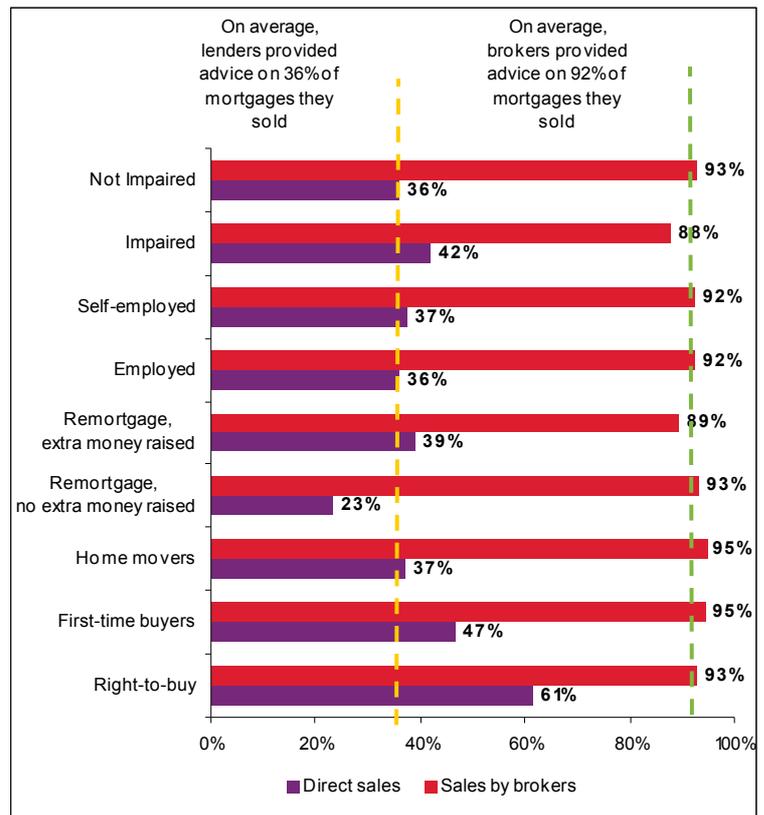
Exhibit 20.11: Advised sales by channel – time trend



Source: FSA PSD

- The level of advice provided by lenders is somewhat higher for higher-risk borrowers or products with higher-risk characteristics. But there is still a considerable proportion of consumers who do not receive advice through lenders.

Exhibit 20.12: Proportion of mortgages sold with advice, by channel and borrower type, 2007



Source: PSD FSA

- Overall, there seems to be no direct relationship between risk and provision of advice in the mortgage market. Some of the riskiest products were sold without advice.

Exhibit 20.13: Provision of advice, by risk type

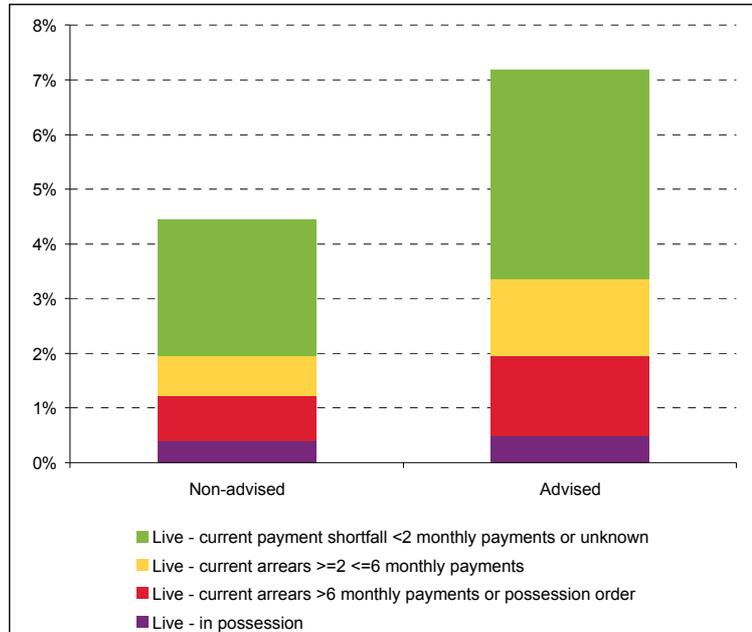
Risk type	Credit impaired	LTV >=80%	Self-employed	Debt consolidation	Right-to-buy	Non-advised sales in total, %
1	NO	NO	NO	NO	NO	38%
2	NO	YES	NO	NO	NO	28%
3	NO	NO	YES	NO	NO	30%
4	NO	NO	NO	YES	NO	29%
5	NO	NO	NO	NO	YES	18%
6	NO	YES	NO	YES	NO	21%
7	NO	NO	YES	YES	NO	20%
8	NO	YES	YES	NO	NO	18%
9	NO	YES	NO	NO	YES	20%
10	NO	NO	YES	NO	YES	14%
11	NO	YES	YES	YES	NO	12%
12	YES	NO	NO	NO	NO	25%
13	NO	YES	YES	NO	YES	15%
14	YES	YES	NO	NO	NO	19%
15	YES	NO	NO	YES	NO	20%
16	YES	NO	YES	NO	NO	20%
17	YES	YES	NO	YES	NO	19%
18	YES	NO	NO	NO	YES	9%
19	YES	NO	YES	YES	NO	17%
20	YES	YES	YES	NO	NO	15%
21	YES	YES	NO	NO	YES	9%
22	YES	YES	YES	NO	YES	11%
23	YES	YES	YES	YES	NO	18%
24	YES	NO	YES	NO	YES	12%
Total						33%

Note: (1) Mortgage sales made in April 2006 to December 2011. (2) Full illustration on risk combinations is available on Exhibit 6.9.

Source: PSD Performance data 2012

- Overall, non-advised sales perform somewhat better.

Exhibit 20.14: Mortgage performance, advised and non-advised sales (current arrears and payment shortfalls)

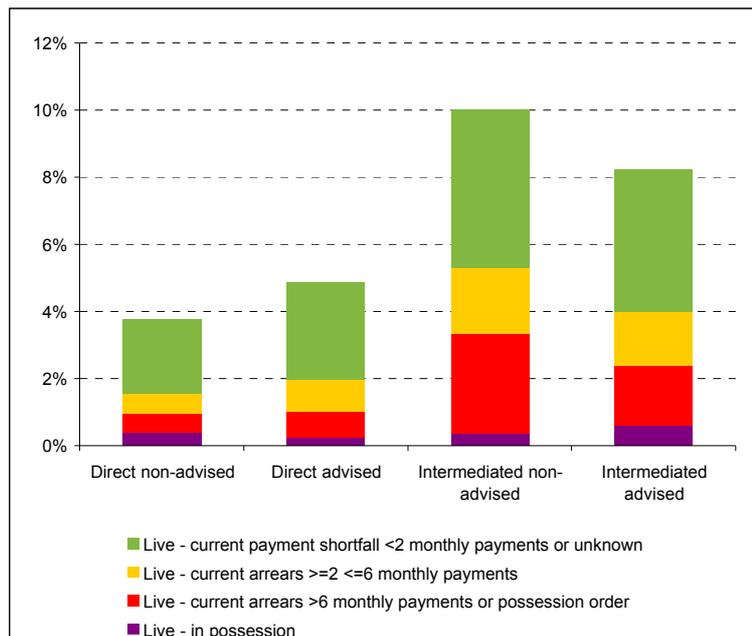


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured.

Source: PSD Performance data 2012

- The performance, however, varies by channel.
- Among direct sales, non-advised (information-only) sales overall perform better than advised sales.
- For broker sales, the picture is reversed, with non-advised sales performing worse in comparison with advised.
- However, in all cases, broker sales, advised or not, appear to perform worse in comparison with direct sales.

Exhibit 20.15: Mortgage performance, advised and non-advised sales, by channel (current arrears and payment shortfalls)

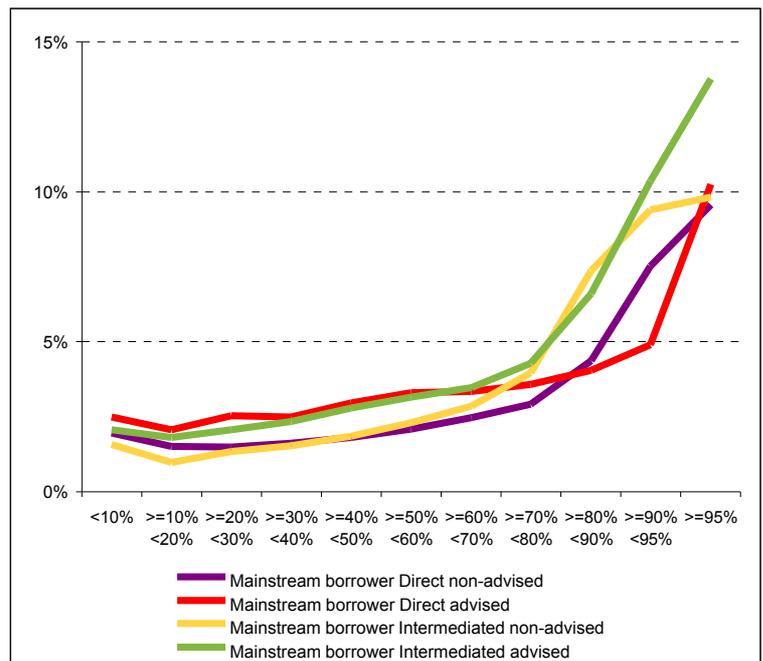


Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured

Source: PSD Performance data 2012

- Some of these differences can be explained by the risk profile of borrowers who choose to borrow direct or via a broker.
- There is not much difference in mortgage performance of mainstream borrowers, regardless of the channel of sale and provision of advice, with both direct and broker sales performing marginally worse where advice was provided.
- This could be because of self-selection of borrowers who choose to obtain advice.
- However, for higher-risk borrowers, which we define here (for illustration purposes only) as those who were credit-impaired, consolidated debts, exercise right-to-buy or borrowed from specialist lenders, there is a considerable difference in the performance of broker sales, with non-advised sales performing considerably worse in comparison with advised.
- However, only a small proportion of broker mortgage sales are non-advised, so the trends we observe could be the consequence of the small sample size.
- For higher-risk borrowers, advised sales by brokers also performed worse in comparison with direct sales.
- We did not identify large differences in the performance of advised and non-advised sales to higher-risk borrowers directly by mortgage providers.

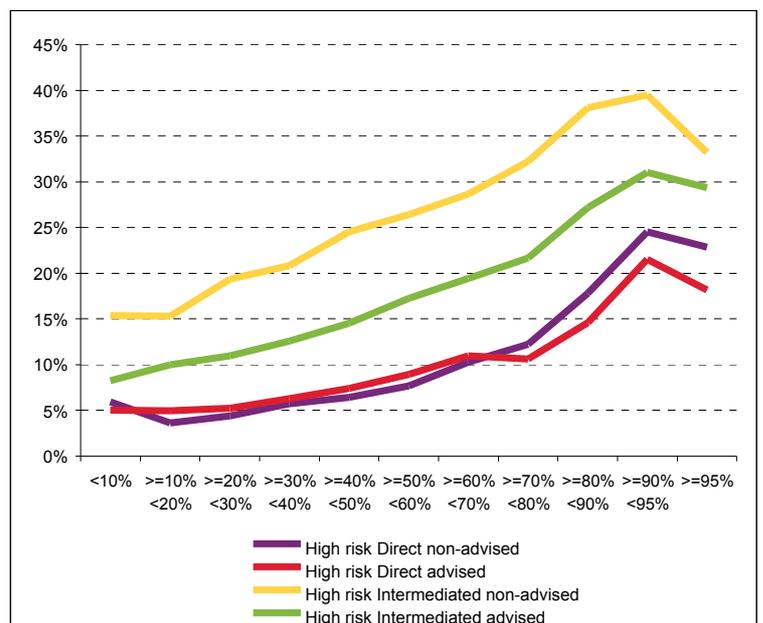
Exhibit 20.16: Mortgage performance, by channel and provision of advice (mainstream borrowers – current arrears and payment shortfalls)



Note: This Exhibit shows performance of mortgages sold in April 2005 - December 2011 that were outstanding as at March 2012 when performance was measured

Source: PSD Performance data 2012

Exhibit 20.17: Mortgage performance, by channel and provision of advice (higher-risk borrowers – current arrears and payment shortfalls)



Source: PSD Performance data 2012

PART V

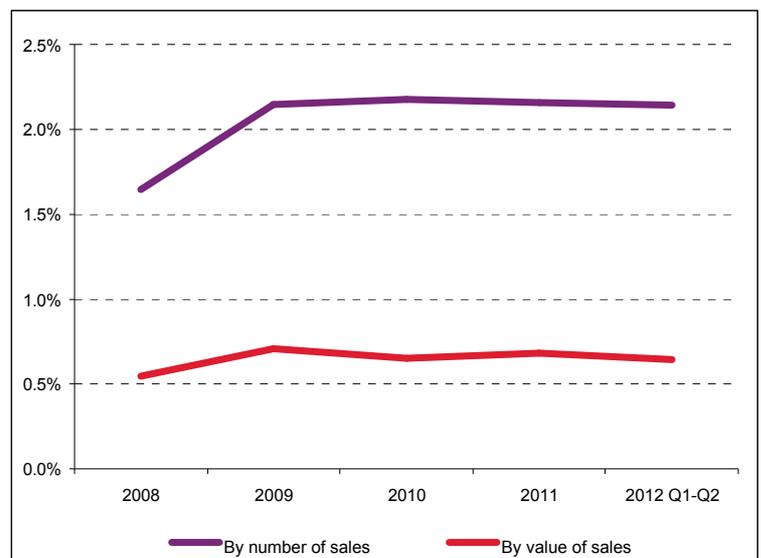
Niche markets

21

Equity release

- Equity release accounts for a very small proportion of regulated mortgage sales – at present, around 2.1% by the number of sales and 0.6% by the value of sales. In 2011, there were just over 19,000 equity release sales worth £840m.
- Mintel estimates that 2% of home owners aged 55+ have an equity release mortgage.²²

Exhibit 21.1: Share of equity release sales in total mortgage sales

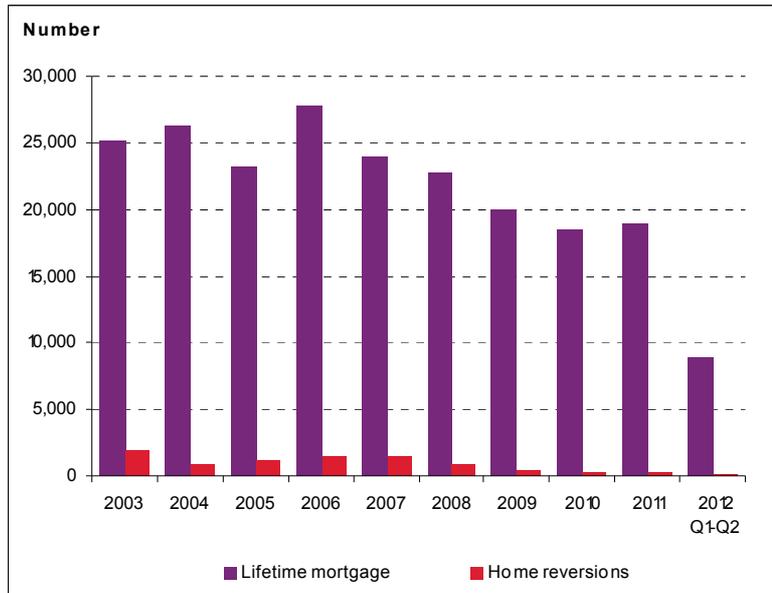


Source: FSA PSD

²² Mintel, Equity Release, UK, May 2011

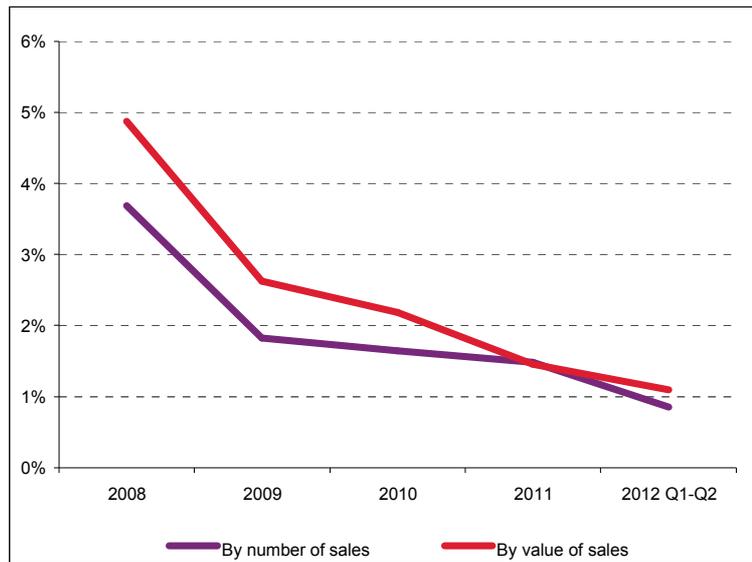
- Most equity release products are lifetime mortgages. Currently, only around 1% of all equity release sales are home reversion plans.

Exhibit 21.2: Number of equity release sales, by type



Source: FSA PSD (2006-2012 for lifetime mortgages, 2008-2012 for home reversion), SHIP & CML (earlier periods)

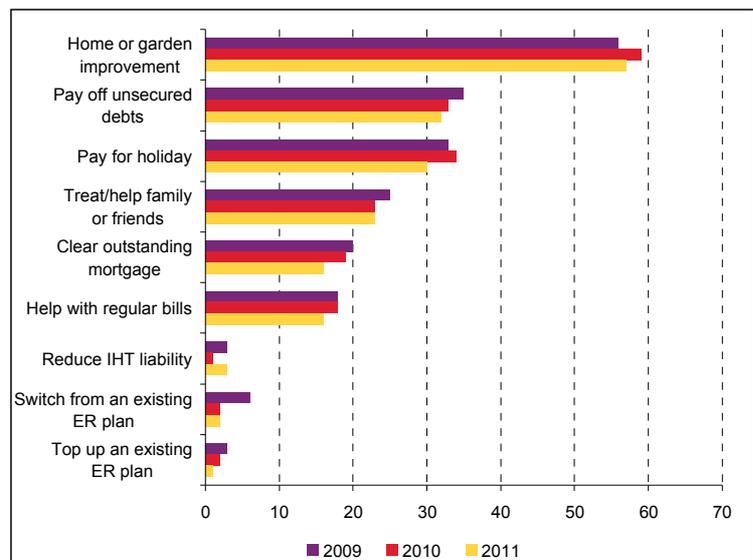
Exhibit 21.3: Share of home reversions in total equity release sales



Source: FSA PSD

- In simple terms, equity release products allow older consumers to access the equity tied up in their homes. These products are typically used to support lifestyle in retirement, including clearing debts.

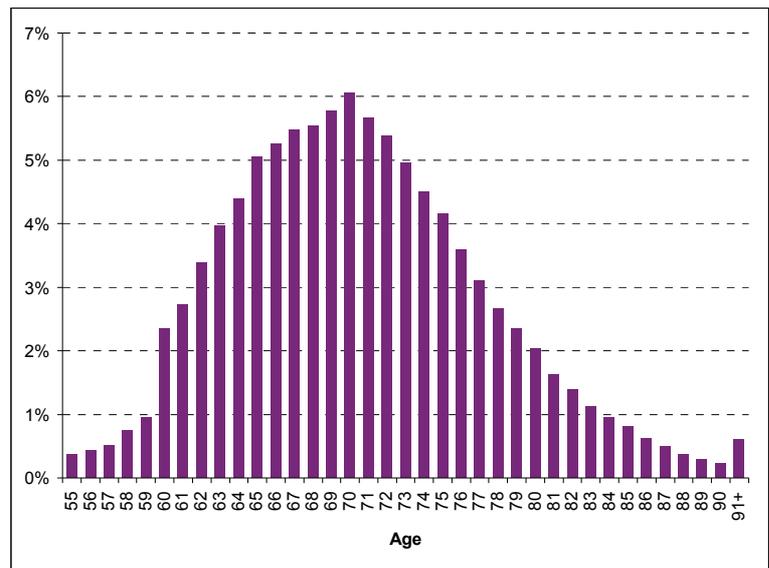
Exhibit 21.4: Popular uses of equity release, 2009-2011



Source: Key Retirement Solutions (reproduced from Mintel, Equity Release, UK, May 2012)

- The average age of a lifetime mortgage borrower currently stands at 70, with the majority of borrowers (90%) being between 60 and 81 years-old.
- Although we do not collect data on borrowers' age for home reversions, we believe that the age of borrowers using this product is similar.

Exhibit 21.5: Age distribution of lifetime mortgage borrowers, April 2005 to June 2012



Source: FSA

- An average, LTV on a lifetime mortgage is around 20%. However, generally, the older the borrower, the more equity they can expect to release from their property.

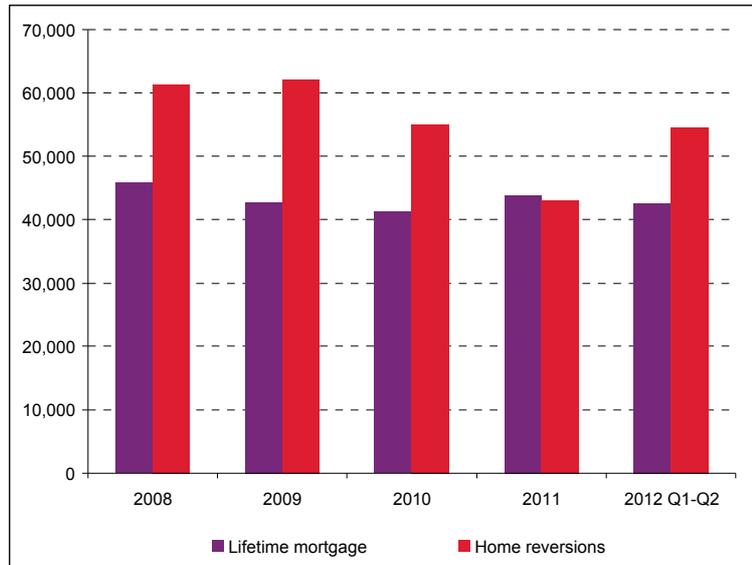
Exhibit 21.6: Average LTV on lifetime mortgages, April 2005 to June 2012



Source: FSA PSD

- Typically, a borrower can take out a higher proportion of equity via a home reversion plan than via a lifetime mortgage. Therefore, home reversion plans, on average, are somewhat larger.
- In Q2 2012, the average size of a home reversion plan was £55,000 and the average size of a lifetime mortgage was around £43,000.

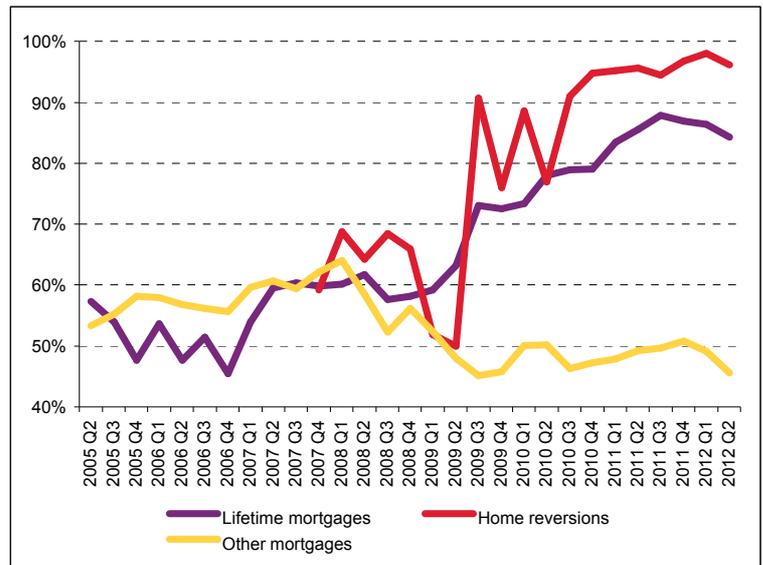
Exhibit 21.7: Average £ value of equity release product, by type



Source: FSA PSD

- The majority of equity release products are sold by brokers: in Q2 2012, 84% of lifetime mortgages and nearly all home reversions (96%).
- The share of brokers in the equity release market has been increasing from 2008 (we note that over the same period, the share of brokers in the sales of mortgages not involving equity release has decreased).

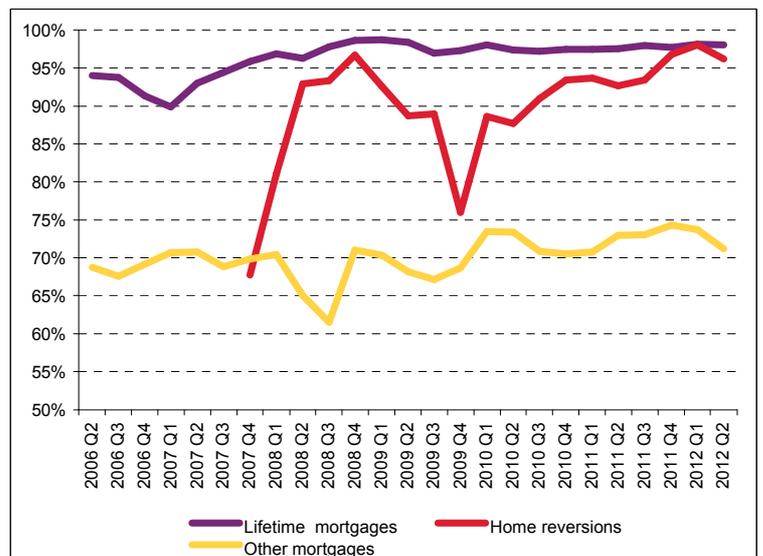
Exhibit 21.8: Share of broker sales in total, by type of product



Source: FSA PSD

- Most equity release sales are advised. For example, in Q2 2012, 98% of lifetime mortgages and 96% of home reversions were advised (compared with 71% of advised sales for mortgages not involving equity release).

Exhibit 21.9: Share of advised sales in total, by type of product

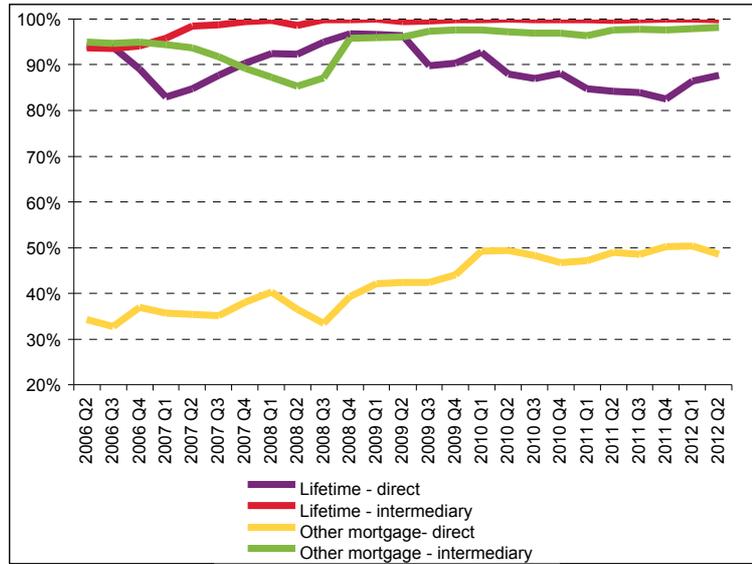


Note: the proportion of advised sales in home reversions is volatile because of the very small number of transactions in each period.

Source: FSA PSD

- As we noted in previous chapters, brokers are more likely to sell mortgages with advice. This is true for equity release too. However, because members of the equity release trade body, Safe Home Income Plans (SHIP), only accept advised sales, the majority of borrowers receive advice, regardless of the sales channel they use.

Exhibit 21.10: Share of advised sales in total, by type of product and channel of sale



Note: The channel and advice split for home reversions is not shown due to a very small number of direct home reversion sales.

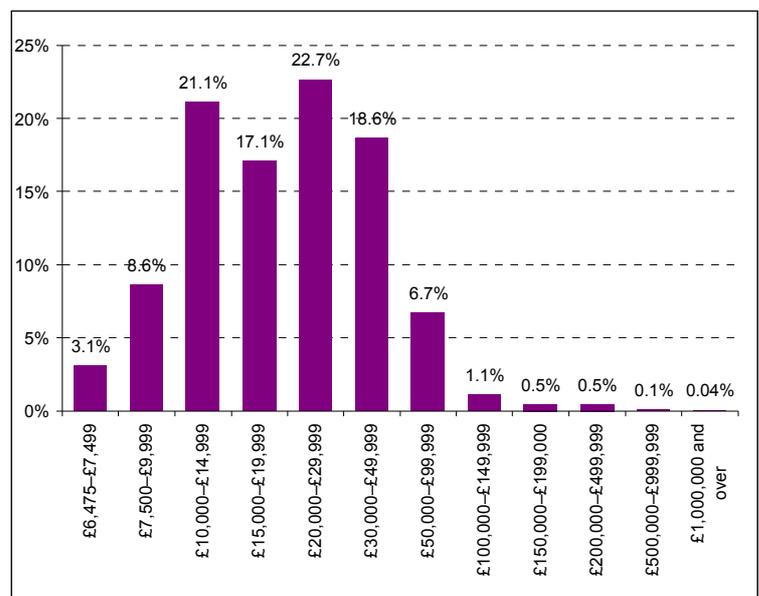
Source: FSA PSD

22

High net worth lending

- Individuals with very high incomes and wealth account for a relatively small proportion of the UK population.
- In 2010/11 around 0.14% had incomes of £500,000 and over.
- Only 0.04% of taxpayers had incomes over £1m a year in 2010/11.

Exhibit 22.1: Distribution of total income of individuals for income tax purposes, including earned and investment income, 2010/11

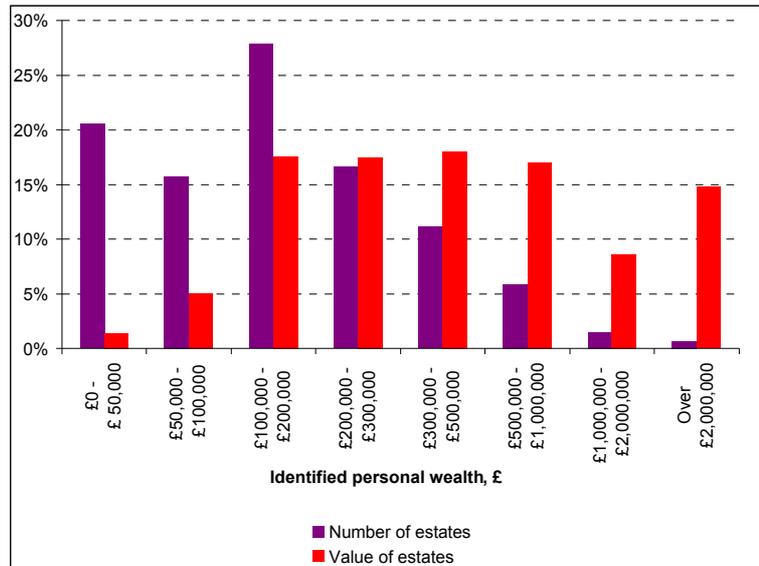


Note: Figures relate to taxpayers only

Source: ONS

- In 2008-2010 only 0.65% of estates had a net value in excess of £2,000,000.

Exhibit 22.2: Total net capital value of estates: distribution by number and £ value, 2008 - 2010

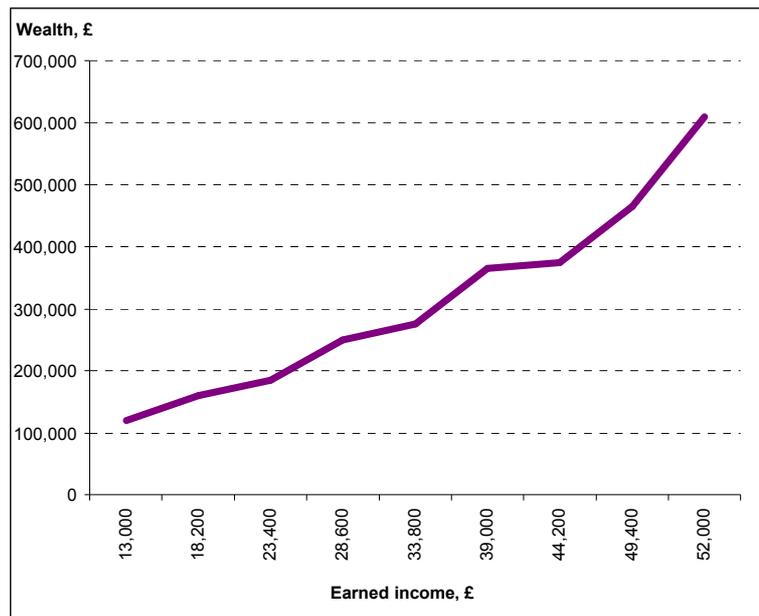


Note: Based on the wealth owned by estates represented by those passing through probate in each year. For 2008 to 2010 this covers 31% of estates.

Source: HMRC

- To get an idea of what the relationship between income and wealth of the HNW may look like for our proposed regulatory definition, we had to make a projection from the available ONS data on households with much smaller incomes and wealth.

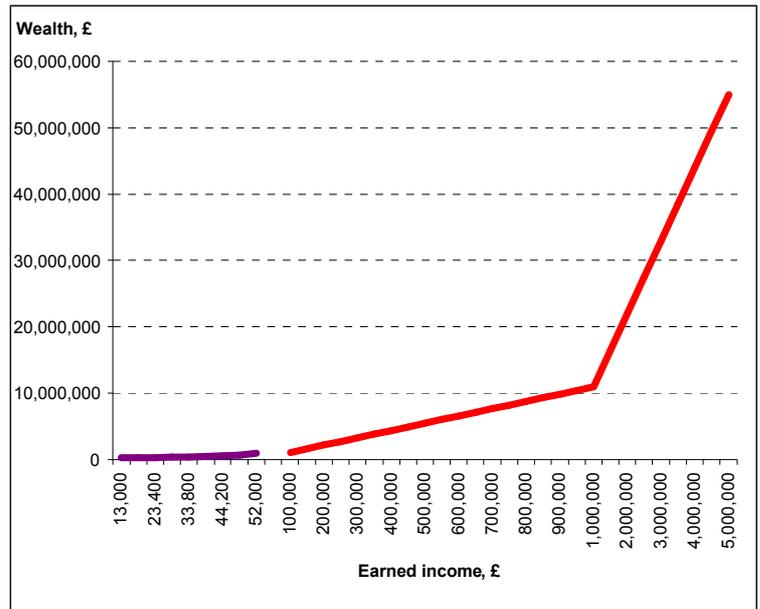
Exhibit 22.3: Relationship between annual earned income and median wealth



Source: ONS, FSA estimate

- This projection assumes that the statistical relationship between income and wealth for HNW is the same as for individuals with lower income and wealth (we used a linear regression model to estimate this). We do not know if our projection is accurate as we have no data to check it against

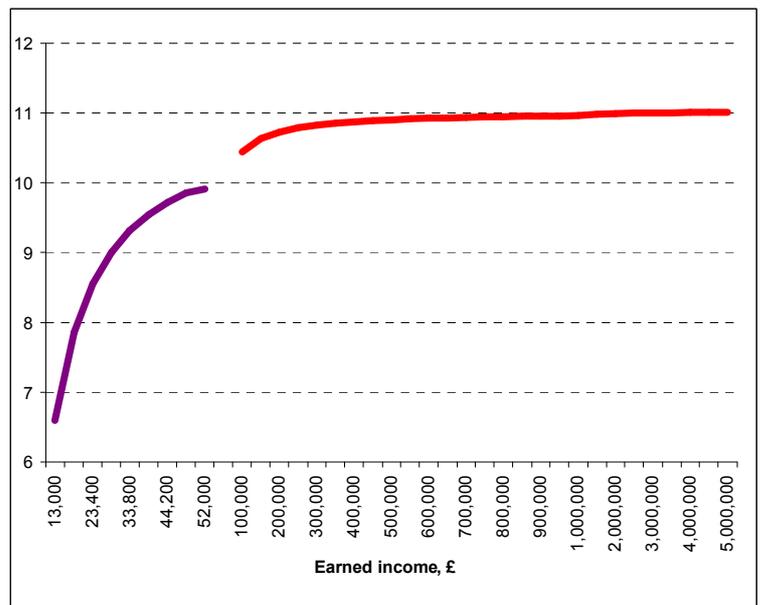
Exhibit 22.4: Relationship between annual earned income and median wealth: projection for higher earners



Source: ONS, FSA estimate

- From our projection, we estimate that, on average, wealth amounts to around 11 times the gross annual income of the individual earning more than £100,000 a year. This relationship is, of course, approximate, and would depend, for example, on an individual's age, personal circumstances and sources of wealth.

Exhibit 22.5: Earned annual income and wealth multiple



Source: ONS, FSA estimate

- Taking individuals with estimated net annual incomes of £300,000 pounds or more, we show how mortgages to HNW could be different from mainstream market²³.
- For example, HNW are more likely than other borrower types to have interest-only mortgages.

Exhibit 22.6: Mortgages to households with net annual incomes of £300,000 pounds or more

Measure	2005 (Q2-Q4)	2006	2007	2008	2009	2010	2011	2012 (Q1-Q2)
Number of sales	1,612	3,015	3,580	2,492	1,789	1,579	1,591	638
% in total number of sales	0.10%	0.13%	0.17%	0.18%	0.20%	0.19%	0.19%	0.16%
Value of sales, £m	1,755	3,454	4,592	3,237	2,079	2,164	2,485	1,129
% in total value of sales	0.89%	1.20%	1.60%	1.65%	1.72%	1.83%	2.05%	1.94%
Average mortgage amount, £	1,088,909	1,145,454	1,282,640	1,298,884	1,162,251	1,370,198	1,561,674	1,768,855
Average mortgage term, years	16	16	17	15	12	11	11	10
Average LTV	47	47	58	46	48	43	45	41
Proportion of interest-only sales	81%	85%	86%	87%	80%	78%	80%	79%

Source: FSA PSD

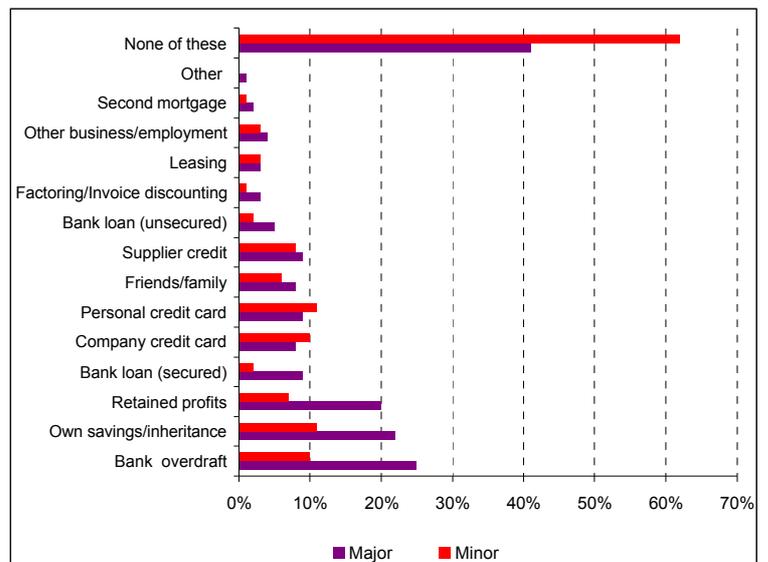
²³ This is an illustration only. We explain in Annex 1 how we have worked out net incomes. Specifically, we were unable to identify elements of gross income taxed differently from earnings, e.g. where tax on dividends or capital gains tax was payable instead of income tax. We were also unable to account for the value of assets the borrowers had as the data was not available to us. This means that not all high net worth borrowers were included in this illustration, e.g. those with more complex tax arrangements or those meeting our HNW definition based on the value of assets.

23

Regulated business mortgages

- We do not have comprehensive data on regulated business lending, so we use surveys to illustrate the extent to which mortgages could be used for a business purpose.
- The data from the Federation of Small Businesses (FSB) suggests that 11% of business owners could be using secured bank loans, with 9% using them to raise long-term capital and 2% to raise short-term finance.
- We know from the ONS data that 13% of all mortgage borrowers are self-employed. This means that around 1.4% of all mortgage borrowers could be using regulated mortgages to fund businesses.

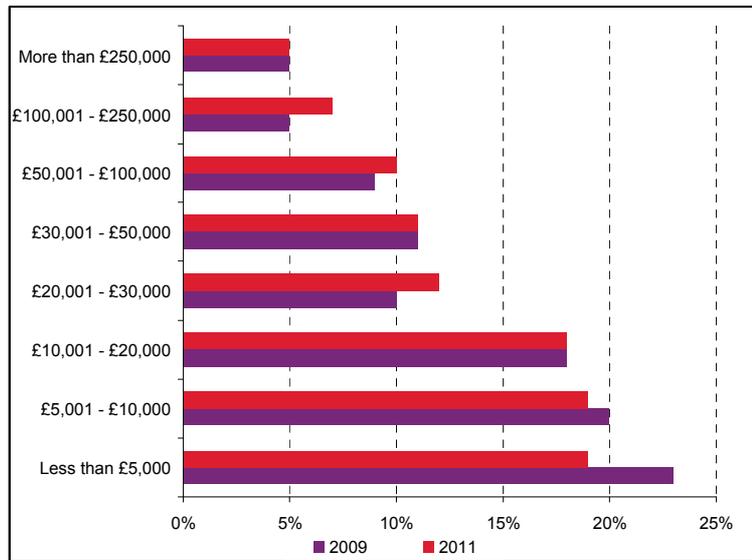
Exhibit 23.1: Sources of business finance



Source: FSB 'Voice of Small Business' Member Survey 2011

- The research by FSB also tells us that around 60% of those who took out loans in 2011 borrowed £20,000 or less.

Exhibit 23.2: Amount borrowed in finance over a year



Source: FSB 'Voice of Small Business' Member Survey 2011

Annex 1

Notes on data and methodology

Data from the FSA regulatory reporting

1. In this paper, we use statistics from our mortgage lending regulatory reporting – Product Sales Data (PSD) and Mortgage Lending and Administration Return (MLAR).¹
2. **Product Sales Data (PSD):** Since 1 April 2005, product providers have been required to provide the FSA with transaction-level data on all sales of regulated mortgage contracts. Between April 2005 and June 2012 around 220 firms reported mortgage sales. Details of loans for house purchases and remortgages are captured by mortgage PSD, but data relating to further advances is not. Additionally, mortgage PSD only covers regulated mortgage contracts and therefore excludes products such as second-charge lending, commercial and buy-to-let mortgages.
3. **Mortgage Lending and Administration Return (MLAR):** Since the beginning of 2007, around 300 regulated mortgage lenders and administrators have been required to submit an MLAR each quarter, providing aggregate data about their mortgage lending and administration activities.
4. All Exhibits based on PSD are on regulated mortgages only. The estimates in this paper exclude equity release, Home Purchase Plans and regulated business mortgages, unless explicitly stated.
5. Some totals may show slight discrepancies due to rounding of figures.

1 Summary statistics from these returns are available on the FSA web-site:
PSD trend reports:
www.fsa.gov.uk/Pages/Doing/Regulated/Returns/psd/publications/index.shtml
Statistics on mortgage lending (MLAR):
www.fsa.gov.uk/pages/Library/Other_publications/statistics/index.shtml

Mortgage performance data

Dataset

6. At present, we do not collect transactional data on mortgage performance as part of regulatory reporting, although the aggregate statistics are collected in MLAR.
7. To establish how the mortgages recorded in PSD have performed, we have collected additional information on a voluntary basis from a sample of lenders. We did this in 2009 and then again in 2011 and in 2012.² This is the most comprehensive source of transactional mortgage arrears data that is available to the FSA.
8. PSD Performance data collected in 2009 shows the performance of mortgages sold between April 2005 and March 2009 by a sample of 33 PSD reporting lenders and covers around 70% of all regulated sales made in this period, with the performance measured as at August 2009. This dataset included 5.4m mortgages of which 4.5m were thought to be outstanding.³
9. PSD Performance data collected in 2011 shows the performance of mortgages sold between April 2005 and September 2010 by a sample of 46 PSD reporting lenders and covers around 80% of all regulated sales made in this period, with the performance measured as at December 2010 to February 2011.⁴ This dataset included 7m mortgages of which 4.3m were outstanding. Note that, unlike with 2009 data, we did not have to make assumptions as to which mortgages were still outstanding, as this time lenders reported this data to us.
10. PSD Performance data collected in 2012 shows performance of mortgages sold between April 2005 and December 2011 by a sample of 54 PSD reporting lenders and covers around 80% of all regulated sales made in this period, with the performance measured as at March 2012.⁵ This dataset included 7.8m mortgages of which 4.7m were outstanding.
11. In 2009, 2011 and 2012, we collected data on missed payments, i.e. payment shortfalls and arrears, and also on repossessions. In 2011 and 2012, we also collected data on historic payment problems and on some types of forbearance. We also asked lenders to tell us which of the mortgages were still active and what their key current characteristics were (i.e. outstanding balance, repayment method, term and interest rate) so that we could see how these had changed since the mortgage was sold. In 2012, we also asked lenders to report on the current interest rate type (e.g. if it was fixed or variable) and on the maximum amount of arrears that the borrower has accrued historically.
12. We matched PSD and performance data into one combined dataset. From this dataset, we can tell how mortgages sold since April 2005 have performed. We can also establish links between the performance and various mortgage and borrower characteristics available in PSD.

2 See Annex 2 for our 2012 data request.

3 See CP10/16, Annex 3 for the assumptions we made to identify outstanding mortgages (www.fsa.gov.uk/pubs/cp/cp10_16.pdf).

4 Although in the data request we asked lenders to report performance data as at 1 December 2010, in practice some lenders reported as at a later date. As a result, the data we have reflects mortgage performance as at December 2010 to February 2011.

5 As above, some lenders may have reported as of a somewhat later date.

13. The following are the advantages of the PSD Performance data collected in 2012:
- complete flexibility (the data is transactional);
 - performance of outstanding mortgages, as well as performance of sales can be measured;
 - contains a record of current (live) and historic (past) arrears;
 - contains a record of capitalisations, formal arrangements and temporary concessions⁶; and
 - it is possible to identify payment difficulties and forbearance cases outside of conventional definitions (for example, payment shortfalls less than two months, or switches from capital repayment to interest-only mortgage – a widely used forbearance option).
14. This data also has limitations:
- only the performance of mortgages sold between April 2005 and December 2011 is captured;
 - not all lenders were able to report all of the data fields, particularly related to historic arrears and forbearance, which means that the data on these is incomplete;
 - the arrears levels measured for outstanding mortgages are better quality than the arrears measured for sales, as some lenders had difficulty reporting performance of closed accounts;
 - although we were able to identify and measure performance of some sold books, there are sold books which are still unaccounted for (this only affects performance of sales and does not affect performance of outstanding mortgages); and
 - it is not possible to establish when exactly some forms of forbearance (capitalisations of arrears and concessions) were granted and whether they still apply.
15. The data collected in 2009, 2011 and 2012 may not be directly comparable due to the differences in the sample, questionnaire and quality of reporting. Therefore, the year-on-year differences in the data may not necessarily represent a time trend.

⁶ MLAR defines capitalisations, temporary concessions and formal arrangements as follows:

- (a) **Capitalisation** is a formal arrangement agreed with the borrower to add all or part of a borrower's arrears to the amount of outstanding principal and then treating that amount of overall debt as the enlarged principal. This enlarged principal is then used as the basis for calculating future monthly payments over the remaining term of the loan.
- (b) **Temporary concession** is an agreement with the borrower whereby monthly payments are either suspended or less than they would be on a fully commercial basis for a period.
- (c) **Formal arrangement** means an agreement to capitalise arrears, which also includes within the term 'arrangement' the example of a borrower making increased monthly payments to reduce some or all existing arrears.

Definitions of mortgage performance categories

16. We use the following definitions of mortgage performance in this paper⁷:
- Borrowers have mortgage **payment shortfalls** if they are less than two⁸ months⁹ behind with their payments.
 - Borrowers are in mortgage **arrears** if they are two or more months behind or if there is a possession order. In this paper, we identify current and historic arrears. We split current arrears into two bands: **current early to medium-term arrears** ($\geq 2 \leq 6$ months) and **current severe arrears** (> 6 months or a possession order). We are unable to split historic arrears into bands, so we present them as a single category of **past arrears** of two or more months.
 - Borrower has had **repossession** if a lender has taken possession of the property that was the subject of the regulated mortgage contract.
 - Borrower benefits from **forbearance** if the lender reported any of the MLAR forbearance options (capitalisations of arrears or temporary concessions)¹⁰, or if we have identified from the data that a borrower with a past record of payment problems switched to a cheaper repayment method (e.g. from a capital repayment basis to interest-only) or extended a mortgage term by five years or more.
 - A **performing mortgage** is a mortgage where we have no record of past payment shortfalls, arrears, reported MLAR forbearance or repossession.

Methodology of some estimates

Risk combinations

17. We used multiple binary logistic regression to identify the risk factors that increase probability of mortgage payment difficulties. We then used combinations of the top five product and borrower-related risk factors to define 24 risk types, as shown in Exhibit 6.9.
18. The risk factors we took into account were impaired credit history of the borrower, higher LTV (set at $LTV \geq 80\%$), self-employment, remortgage for debt consolidation and where a social tenant exercised their right-to-buy.

7 Note that these definitions are different from the definitions used in CP10/16 as the structure of the data collected in 2011 and in 2012 is different.

8 Some payments can be missed for technical reasons and not because of payment problems. For example, this may happen due to lenders' technical error or because borrower's direct debit information was incorrect. We are unable to identify technical missed payments in our data, so the payment shortfalls statistics that we show could be somewhat overstated. However, we do not expect the proportion of technical cases in total payment shortfalls to be significant.

9 In order to calculate current mortgage payments, we use mortgage balance, mortgage term and interest rate as at March 2012, as reported by lenders.

10 Most lenders in our sample started reporting forbearance in MLAR in 2007, so the earlier data on this is not available. Also, some lenders could not report MLAR forbearance on a transactional basis at all, so our data is incomplete.

19. Although there are five risk factors in our analysis, the maximum number of risk factors that any particular account may exhibit is four. This is because in PSD ‘remortgage for debt consolidation’ and ‘right-to-buy’ (RTB) categories do not overlap (i.e. if a borrower remortgages for debt consolidation, it is not known if they have exercised their RTB in the past; similarly, if a borrower is exercising their RTB for the first time, it is not known if a part of a mortgage is being used for debt consolidation).

Risk scores

20. We use data on risk combinations to calculate risk scores. Risk scores are lender-specific and calculated as follows:
- we worked out book structure for each lender, as per the 24 risk types (total book = 100%); and
 - we then multiplied the proportion of business in each risk type by the relevant weight (risk order). The risk score is the sum of these multiples.
21. Risk score can be between one and 24. The higher the risk exposure taken by the lender, the higher the risk score. In our data, risk scores range from one to 11.¹¹

Types of lenders

22. In a number of exhibits we present data broken down by the following five types of lenders: banks, subsidiaries of banks, building societies, subsidiaries of building societies and non-banks.
23. In this classification, ‘non-banks’ is an illustrative category that identifies lenders with no deposit-taking permissions that targeted specialist markets and were independent of the UK retail banks and building societies. This means that lenders who were subsidiaries of foreign investment banks were classified as ‘non-banks’. Some lenders may have changed their type over the period for which we have data (2005–2012). In such cases, where possible, the type was assigned as it was before 2008.
24. We have excluded the data of lenders that were mainly operating in the niche markets, such as private banking, bridging finance or equity release. The data for these types of lenders is not included in the categories above and is not presented in this paper, unless explicitly stated.

Borrowers who are ‘mortgage prisoners’

25. We looked at outstanding mortgages that started between April 2005 and December 2011 to estimate how many of these borrowers would have found it difficult to remortgage in early 2012 if they wished to do so.

11 Risk score would be 1 if 100% of lender’s business was only to borrowers of type 1. Risk score would be 24 if, on the other hand, 100% of lender’s business was to borrowers showing all of the characteristics identified in type 24. In practice, lenders lent to a mixture of borrowers, so the risk scores in our data range from between just over 1 to just under 11.

26. We have looked at three types of products with the greatest reduction in availability:
- credit impaired;
 - high LTV; and
 - interest-only.
27. We estimate from the current data on product availability, as reported by Moneyfacts, that 100% of credit-impaired borrowers are excluded from the market.¹² For repayment mortgages, we also assume that any borrowers with the current LTV>85% would find it difficult or prohibitively expensive to remortgage (see Exhibits 4.10 and 4.11). For interest-only mortgages, we assume that any borrowers with the current LTV>75%, as well as those with equity <£150,000 or no record of repayment vehicle could find it difficult to remortgage.¹³
28. To estimate how many borrowers are ‘mortgage prisoners’, we, therefore, need to identify those who are:
- likely to be credit impaired; and/or
 - have repayment mortgages and are likely to have current (indexed) LTVs>85%;
 - have interest-only mortgages and are likely to have current (indexed) LTV>75%;
 - have interest-only mortgages, equity <£150,000 or no record of repayment vehicle.
29. For the purposes of this assessment, we assumed that credit-impaired borrowers are those who were credit-impaired at origination, as well as borrowers who have experienced mortgage payment problems at a later stage (as evidenced by the record of arrears or payment shortfalls in our data).
30. We worked out the current indexed LTV for each borrower by taking the current outstanding mortgage amount (which was reported to us by lenders) and dividing it by current indexed property value.
31. To calculate indexed property values, we used statistics on average regional property prices by Halifax, Nationwide and Acadametrics to estimate how much each mortgaged property was worth in Q1 2012. We used the property value at origination from PSD as a basis for this calculation (so we assumed that property valuation at the time of mortgage application was correct). We then worked out an index at which the property price could have increased or decreased by Q1 2012. For example, for a borrower who has taken out a mortgage in Q1 2007, with recorded property value of £100,000 in East Anglia, we estimate that in Q1 2012 this property could be worth $£100,000 \times 0.905 = £90,500$ using Halifax house price index, or $£100,000 \times 0.888 = £88,800$ using Nationwide house price index, or

12 In practice, a few credit-impaired products are probably still available.

13 These criteria were selected based on the mortgage product availability in the first half of 2012.

$£100,000 \times 0.968 = £96,800$ using Acadametrics house price index. As house price indices vary, sometimes significantly, we present all three estimates side by side.

32. In reality, not all borrowers with LTVs in excess of 85% are trapped and not all borrowers with a record of missed payments are excluded from the market. Also, as our data on repayment strategies of interest-only borrowers is limited to ISAs, endowments and pensions, and is therefore incomplete, we are probably overstating the proportion of interest-only borrowers that would find it difficult to remortgage. On the other hand, some borrowers may have developed a credit impairment unrelated to a mortgage (e.g. they may be in arrears on their credit cards or personal loans) and therefore may find it difficult to obtain new mortgages, but they will not be included in our estimates. Also, some borrowers with LTVs just below 85% may find mortgages available at this level of LTV expensive, so may also feel ‘trapped’.

Borrowers in negative equity

33. An extension of the analysis of ‘mortgage prisoners’ is the analysis of negative equity. We say that the borrower is in negative equity if their current indexed LTV > 100%. We explain in section *Borrowers who are ‘mortgage prisoners’* how we have worked out indexed LTVs.

Income- and expenditure-related estimates

Income tax and National Insurance (NI) contributions

34. For taxation purposes, where joint income is reported in PSD, we assumed that individual incomes were 50% of the total. Where the borrower type was ‘self-employed’ and the income was joint, we have assumed that the first borrower is self-employed and the second borrower is employed.
35. Income tax and NI contributions were worked out using rates and personal allowances for the relevant tax year when the mortgage was originated. We took into account age-related personal allowances. In PSD we are unable to identify elements of gross income taxed differently from earning, e.g. where tax on dividends or capitals gains tax was payable instead of income tax, or where no tax was payable, such as child benefits or interest on ISAs. Therefore, we calculated taxes and NI based on the total gross incomes.
36. We deducted Class 1 NI for employed borrowers and Class 2 and 4 NI for self-employed borrowers. We applied small earnings allowance to the NI contributions paid by self-employed borrowers where applicable. We have not deducted NI contributions for retired borrowers.
37. We have not applied Class 3 NI to any borrowers and have not estimated the amount of any contributions to pension funds, saving accounts, or to repayment vehicles for interest-only mortgages.

Contractual mortgage payments

38. We have calculated contractual mortgage payments at origination and as at March 2012, based on the mortgage characteristics at the point of mortgage sale and as at March 2012 respectively, including the mortgage type, amount, term and interest rate. Where the mortgage type is a ‘mix of interest-only and repayment’ we have assumed that 50% is on a repayment basis and 50% is on an interest-only basis (the exact split is not collected in PSD). As mortgage interest rates at origination are an optional reporting requirement, our estimates at the point of mortgage sale are based on the sub-set of mortgages where the interest rate was reported.

Amount of money available for non-mortgage expenditure

39. We have calculated the amount of money available for non-mortgage expenditure by deducting income tax, NI and the contractual mortgage payment at origination from reported gross income.

Estimates from Living Costs and Food Survey/Expenditure and Food Survey

40. The Living Costs and Food Survey (LCF), previously known as the Expenditure and Food Survey (EFS), is an annual survey conducted by the Office of National Statistics (ONS). It contains data on household expenditure and income¹⁴ and is used to compute some key national statistics, such as the Retail Price Index (RPI) and household final consumption expenditure – the latter, in turn, feeds into the National Accounts and estimates of GDP.
41. We used the data collected in the 2005-2010 surveys to assess the expenditure of those borrowers with a mortgage.
42. We used the data on gross incomes¹⁵ to construct income deciles.
43. As 2011–2012 LCF data was not available at the time of this publication, we estimated expenditure and income deciles in 2011 and 2012 by adjusting 2010 data for changes in CPI and average earnings.
44. We calculated the non-mortgage expenditure of households by deducting mortgage interest¹⁶ from the total expenditure.^{17, 18}

14 LCF/EFS income data does not include use of savings or credit, payouts by insurance policies, proceeds from the sale of assets and windfalls (such as winnings from betting or legacies). Expenditure, however, might reflect these items. More information on the Survey data and limitations is available on the ONS website. For example, see www.ons.gov.uk/ons/rel/family-spending/family-spending/family-spending-2011-edition/index.html

15 Variable p344p ‘Gross normal weekly household income’.

16 Depending on mortgage type – variable B130 ‘Mortgage interest only – last payment’ or variable B150 ‘Mortgage interest/principle – interest paid’.

17 The list of expenditure items collected in LCF/EFS can be found in ONS publications. For example, see Table A1 in ‘Family Spending: a report on the 2010 Living Costs and Food Survey’ available at www.ons.gov.uk/ons/rel/family-spending/family-spending/family-spending-2011-edition/index.html.

18 Variable P630tp ‘EFS: Total Expenditure (anonymised)’.

45. We then calculated whether there was an income shortfall or surplus by taking normal disposable income¹⁹ and deducting from that non-mortgage expenditure and total mortgage payments.²⁰

Expenditure and mortgage affordability: methodology

46. There are many factors that define the level of household expenditure, such as family composition, the socio-economic status of the household and the type of tenure.²¹ Household composition and socio-economic status, which are the strongest predictors of the level of household expenditure²², are not available in PSD.
47. While there are no variables in PSD that could be used as a reliable proxy for household composition²³, the level of gross income, on the other hand, can be a useful alternative to the socio-economic status of the household.²⁴ We can also account for the differences in expenditure by tenure by simply looking at expenditure of the households with a mortgage from LCF/EFS.
48. In the absence of transactional-level data on non-mortgage expenditure in PSD, we are unable to assess with accuracy the retrospective affordability of individual mortgages. However, as the general structure of the PSD dataset, as measured by gross income deciles, is largely consistent with the structure of the LCF/EFS dataset (which means that the socio-demographic structure of the two datasets is similar), we would expect that the distribution of expenditure of the households captured in PSD would be similar to that in the LCF/EFS, when controlling for the relevant year and income deciles.
49. We therefore calculated the median non-mortgage expenditure for each income decile and year from the LCF/EFS dataset and imputed it in the PSD.
50. In the LCF/EFS dataset, given the definition of the median, 50% of households have non-mortgage expenditure below the median expenditure for their income group and year and 50% above. In the PSD, if all mortgages, on average, were affordable at origination, we would expect to see a similar distribution of the money available for non-mortgage expenditure around the LCF/EFS median non-mortgage expenditure. However, if the distribution contained more or less than 50% of accounts on any one side, this could mean the following:

19 Variable P389p 'Normal weekly disposable household income – anonymised'.

20 Depending on mortgage type – variables B130 'Mortgage interest only – last payment', or B200 'Mortgage interest/principle – last payment', or B203 'Mixed mortgage – last payment'.

21 For example, see Chapter 5 of the 'Family Spending 2009 edition: a report on the Living Costs and Food Survey 2008' available at www.ons.gov.uk/ons/rel/family-spending/family-spending/2009-edition/family-spending.pdf

22 We do not use age of the household reference person and the urban / rural location of the household because the impact of both is relatively small.

23 The only variable that carries some of this information is 'income basis' which can be 'single' or 'joint' in PSD. However, it can not be used as a reliable measure of the household size as the number of household members supported from the stated income is not reported to us (for example, a declared single income of £30,000 can support a household that consists of one adult or a household that consists of two adults and three dependent children).

24 Indeed, it follows from our analysis of the LCF/EFS data that the level of gross income alone explains 35% of the variance in the level of household expenditure. The two variables are strongly correlated, with the Pearson correlation coefficient of 60%.

- If over 50% of borrowers have more money than their benchmark expenditure median would require, this would indicate that, overall, there was surplus affordability in the market at the time of mortgage origination, i.e. most borrowers could meet their mortgage payments and non-mortgage expenditure in full and could save to provide buffer against possible income shocks in future (such as unemployment).
 - If, however, more than 50% of borrowers were below their benchmark expenditure median, then this would indicate that, overall, some mortgages were unaffordable, as some borrowers would have not had enough money for all of their expenditure, and therefore would have to use savings (if they had any) or further borrowing to supplement their incomes. Such borrowers would be unable to save and would become instantly vulnerable to any future income shocks (such as unemployment). If further borrowing is used to top up income, this would add to indebtedness and increase their vulnerability further.
51. We measured the extent of the difference by comparing the distribution around the median of expenditure collected in LCF/EFS with the distribution of money available for non-mortgage expenditure calculated from PSD. The results of this comparison are shown in Exhibit 9.10.

Acknowledgements

52. We would like to thank the following organisations:
- *mortgage lenders*, for sharing transactional data on mortgage performance;
 - *the Council of Mortgage Lenders*, for collecting and cleaning the data on mortgage performance from lenders on our behalf and for providing access to historic data on the structure of mortgage lending before 2005;
 - *YouGov and Shelter* for sharing their data from 2009, 2010 and 2011 surveys on the financial position of UK households for our analysis; and
 - *Which?* for sharing their research on mortgage borrowers' sensitivity to interest rate increase.
53. The views expressed here are entirely those of the FSA.

Annex 2

FSA PSD: Arrears, possessions, concessions and arrangements data request

1. To be reported

- Regulated first charge mortgages completed on or after 1 April 2005 (i.e. those that have been reported in PSD), that:
 - a) are held on balance sheet;
 - b) have been securitised but are still serviced by the lender or nominated third party; or
 - c) have been acquired from other lenders.
- Where a further loan has been granted since the original PSD transaction was reported, please conflate any further advance with the original loan where possible and reflect in both the current balance outstanding, amount of arrears and other characteristics. Where characteristics of the further advance (other than loan and arrears amount) differ from those for the main loan, characteristics should be reported as applicable to the main loan. Please report any such conflated loans under the original transaction reference number wherever possible.

The effective reporting date is **1 March 2012** and applies to all PSD transactions reported for the period from **1 April 2005 to 31 December 2011**.

If you extract data after 1 March 2012 and if you are unable to back-date your report to 1 March, then please report as at the date of extraction. **Please include the date of extraction with your report.**

2. Data format

Excel (where the number of transactions allows) or .CSV.

An example set of data (in Excel format) is provided as attachments to this request. Data should be provided in this format, whether Excel or .CSV.

3. Data and definitions

3.1. Arrears, possessions, concessions and arrangements

The following regulated loans should be reported in this section:

- 1) accounts where a **possession order** has been obtained or **possession** has taken place, or where a **receiver of rent** has been appointed at any time since the original PSD transaction was reported, regardless of whether or not the account is still active/live on your system (for instance, where the property has been sold under possession and the account closed);
- 2) accounts live on your system that have been in **arrears of any amount at any time since the original PSD transaction was reported**, even if the account was not in arrears at the reporting date; and
- 3) accounts that have been in **arrears** since the original PSD transaction was reported but where the mortgage has been **paid off** and the account closed.

All accounts that are **currently in arrears** should be reported, **regardless of the arrears amount**.

Where an account is **not currently in arrears**, report all of the following accounts:

- a) accounts where an 'arrears letter' was sent to a borrower, as per MCOB 13.4.1, at any time since the original PSD transaction was reported;
- b) accounts where you used a **temporary concession**, as reported in MLAR;
- c) accounts where you used a **formal arrangement**, as reported in MLAR;
- d) accounts where you have **capitalised arrears**, as reported in MLAR; and
- e) accounts that were in **arrears of any amount** at any time since the original PSD transaction was reported, but **where none of the criteria a-d applies**.

Data field	Description
PSD transaction reference number	<p>The same transaction reference number that was used to report the initial PSD transaction.</p> <p>If you acquired a loan from another firm, please report the same transaction reference number as the originating lender reported in its PSD submission. Where this is not available, please use the originating lender's account number for the mortgage. Where neither of these is available, please report the transaction reference number that you currently use. We cannot use this reference to match your data with the PSD, but we can quote it if we need to contact you.</p>
<p>Mortgage and consumer information, as originally reported in PSD:</p> <ul style="list-style-type: none"> <li data-bbox="304 819 683 927">• Date mortgage account opened <i>Date to be reported in format dd/mm/yyyy</i> <li data-bbox="304 938 683 1106">• Date of birth of main borrower (date of birth of first named borrower) <i>Date to be reported in format dd/mm/yyyy</i> <li data-bbox="304 1117 683 1189">• Property postcode (without spaces) <li data-bbox="304 1200 683 1238">• Value of original loan, £ 	<p>We require this information so that we can create a secondary unique transaction identifier. We will use this identifier to check that we have matched your data with your original PSD correctly and to match accounts where the transaction reference number is different from the original transaction reference number reported in PSD (for example, for acquired loans, or where the lender has modified the original reference number for administrative reasons).</p>
Current amount of arrears, £	<p>The actual amount of arrears outstanding on the account at 1 March 2012 (or at the date of extraction). Arrears should be reported as positive numbers, even if for internal purposes your systems show arrears as negative numbers.</p> <p>Definition of arrears – Arrears will arise through the borrower failing to service any element of his/her contractual debt obligation to the firm, including capital, interest, or fees, fines, administrative charges, default interest or insurance premiums.</p> <p>Where the property was sold, whether under possession, by receiver or by borrower, report the amount of arrears immediately before the date of sale, or as close before the date of sale as is available to you.</p> <p>Where any of the criteria set out in Section 3.1 (a) to (e) apply but the account is not currently in arrears, report 0 or leave blank.</p>

Mortgage Market Review Data Pack

Data field	Description
Maximum amount of arrears on record, £	<p>This is the maximum amount of arrears that the customer has accrued at any point between the date of mortgage sale and 1 March 2012 (or the date of extraction). Arrears should be reported as a positive numbers, even if for internal purposes your systems show arrears as negative numbers.</p> <p>Definition of arrears – Arrears will arise through the borrower failing to service any element of his/her contractual debt obligation to the firm, including capital, interest, or fees, fines, administrative charges, default interest or insurance premiums.</p> <p>If the customer is in current arrears and the maximum amount of arrears on record is the current amount of arrears, then report the current amount of arrears here.</p> <p>Note that for accounts reported in Section 3.1, the ‘maximum amount of arrears on record’ cannot be zero. Leave blank if you cannot provide this data.</p>
Date when maximum amount of arrears was recorded	<p><i>The date that relates to the maximum amount of arrears on record reported in the field above.</i></p> <p>If the customer is in current arrears and the maximum amount of arrears on record is the current amount of arrears, then report the current date (i.e., 01/03/2012 or the date of extraction).</p> <p><i>Date to be reported in format dd/mm/yyyy</i></p>
Date of the first ‘arrears letter’	<p><i>Where applicable</i>, the date when the first ‘arrears letter’ was sent to a borrower, as per MCOB 13.4.1. If the borrower has been in arrears more than once, report the date of the first such letter.</p> <p>Note that you should report all accounts where you have sent the ‘arrears letter’, even if they are not currently in arrears.</p> <p><i>Date to be reported in format dd/mm/yyyy</i></p>
Was there a temporary concession to a borrower?	<p>Where applicable, report Y (Yes) for any accounts where there has been a temporary concession at any time since the original PSD transaction was reported.</p> <p>Here, report all accounts that you have included in your MLAR submissions, Forms F5 and H5, Section ‘A temporary concession’, even if they are not currently in arrears.</p>
Was there a formal arrangement with a borrower?	<p><i>Where applicable</i>, report Y (Yes) for any accounts where there has been a formal arrangement at any time since the original PSD transaction was reported.</p> <p>Here, report all accounts that you have included in your MLAR submissions, Forms F5 and H5, Section ‘A formal arrangement’, even if they are not currently in arrears.</p>
Were arrears capitalised at any point?	<p><i>Where applicable</i>, report Y (Yes) for any accounts where you have capitalised arrears at any time since the original PSD transaction was reported.</p> <p>Here, report all accounts that you have included in your MLAR submissions, Forms F5 and H5, Section ‘Capitalisation of arrears cases in quarter’, even if they are not currently in arrears.</p>

Data field	Description
Is there a Possession Order in place?	<p>Where applicable, report Y (Yes) for any accounts where there is a valid Possession Order in place attached to the mortgage.</p> <p>Or instead, you may report the date of the Possession Order, if this is easier.</p> <p><i>Date to be reported in format dd/mm/yyyy</i></p>
Date of possession (or date receiver of rent appointed)	<p>Where applicable, the date the lender took physical possession of the property.</p> <p><i>Date to be reported in format dd/mm/yyyy</i></p>
Current balance outstanding, £	<p>The balance outstanding on the account at 1 March 2012 (or at the date of extraction). This should include any arrears, fees and charges that have accrued and have not yet been paid off. Where a further loan has been granted since the original PSD transaction was reported, please conflate any further advance with the original loan where possible.</p> <p>Where the property was sold, whether under possession, by receiver or by borrower, report the account balance immediately before the date of sale, or as close before the date of sale as is available to you.</p>
Current interest rate, number, 2 decimal places	<p>The interest rate applicable to the account as at 1 March 2012 (or at the date of extraction). Where more than one interest rate applies to the account, report the interest rate applicable to the largest proportion of the mortgage account.</p> <p>Where the property was sold, whether under possession, by receiver or by borrower, report the interest rate applicable immediately before the date of sale, or as close before the date of sale as is available to you.</p>
Term remaining on the mortgage, in months	<p>The remaining term on the mortgage, expressed as the number of whole months, as at 1 March 2012 (or at the date of extraction).</p> <p>Where the property was sold, whether under possession, by receiver or by borrower, report the mortgage term immediately before the date of sale, or as close before the date of sale as is available to you.</p>
Current method of repayment	<p>The current method of repayment applicable to the account as at 1 March 2012 (or at the date of extraction).</p> <p>Use the same coding as in PSD:</p> <ul style="list-style-type: none"> C = Capital and interest E = Interest only/endowment I = Interest only/ISA P = Interest only/pension U = Interest only/unknown M = Mix of 'capital and interest' and 'interest only' N = Not known <p>Where the property was sold, whether under possession, by receiver or by borrower, report the repayment method immediately before the date of sale, or as close before the date of sale as is available to you.</p>

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3.2. All live accounts

To enable us to update our PSD and to identify accounts which were closed and should therefore be excluded from some analysis, please report the following – **in a separate file to the performance data above.**

Please report all loans as specified in Section 1.

Data field	Description
PSD transaction reference numbers of all live accounts previously reported in PSD	Please report transaction reference numbers of all live accounts for regulated mortgages originated since April 2005 held on your balance sheet or in your SPVs as at 1 March 2012 (or at the date of extraction) , regardless of their arrears status.
Mortgage and consumer information, as originally reported in PSD:	We require this information so that we could create a secondary unique transaction identifier. We will use this identifier to check that we have matched your data with your original PSD correctly and to match accounts where the transaction reference number is different from the original transaction reference number reported in PSD (for example, for acquired loans, or where the lender has modified the original reference number for administrative reasons).
<ul style="list-style-type: none"> • Date mortgage account opened <i>Date to be reported in format dd/mm/yyyy</i> 	
<ul style="list-style-type: none"> • Date of birth of main borrower (date of birth of first named borrower) <i>Date to be reported in format dd/mm/yyyy</i> 	
<ul style="list-style-type: none"> • Property postcode (without spaces) • Value of original loan, £ 	
Current balance outstanding, £	The balance outstanding on the account at 1 March 2012 (or at the date of extraction) . This should include any arrears, fees and charges that have accrued and have not yet been paid off. Where a further loan has been granted since the original PSD transaction was reported, please conflate any further advance with the original loan where possible.
Current interest rate, number, 2 decimal places	The interest rate applicable to the account as at 1 March 2012 (or at the date of extraction) . Where more than one interest rate applies to the account, report the interest rate applicable to the largest proportion of the mortgage account.
Current type of interest rate	The current type of interest rate applicable to the account as at 1 March 2012 (or at the date of extraction) . Use the same coding as in PSD: 01 = Fixed rate 02 = Discounted variable rate 03 = Tracker 04 = Capped rate 05 = Standard variable rate 99 = Other. Use this when product is not one of the above.
Term remaining on a mortgage, in months	The remaining term on a mortgage, expressed as the number of whole months , as at 1 March 2012 (or at the date of extraction) .

Data field	Description
Current method of repayment	The current method of repayment applicable to the account as at 1 March 2012 (or at the date of extraction) . Use the same coding as in PSD: C = Capital and interest E = Interest only/endowment I = Interest only/ISA P = Interest only/pension U = Interest only/unknown M = Mix of 'capital and interest' and 'interest only' N = Not known

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