# Assessment of Northern Ireland’s Mortgage Market

**February 2018**

# Contents

# 1. Executive Summary

1.1 In 2016, the Northern Ireland (NI) mortgage market made up only 0.9% of new United Kingdom (UK) mortgage lending[1], while the NI population made making up 2.9% of the total UK population. There is the potential that NI financial services are being overlooked from a regulatory and policy perspective due to its relatively small contribution to the UK market. However, the market structure and economic landscape of NI are quite distinct to Great Britain (GB). Over 20% of the NI mortgage market consists of lenders that do not offer mortgages in GB[2].

1.2 The mortgage market in NI has changed significantly in the last decade. New mortgage lending in NI plummeted from £6.9bn in 2007 to £1.5bn by 2012, rising slightly to £2.4bn by 2016[3]. In the same period, the number of 'active lenders' fell by 36% (from 36 to 23)[4]. A number of metrics suggest the quality of new lending in NI is improving. In 2016, NI first time buyers had a lower loan to income (LTI) ratio than the UK average (2.9 in NI compared to 3.51 for the UK)[5]. The percentage of monthly income servicing capital and interest repayments is also lower (16.2% in NI compared to 18% for the UK)[6]. While first time buyers struggle to get onto the housing ladder in other UK regions, over 60% of regulated house purchases in NI were undertaken by first time buyers in 2016[7].

1.3 The biggest concern for the NI mortgage market is the disproportionate exposure to UK-wide legacy issues, most notably the 2008 Global Financial Crisis (GFC), and the resulting NI house price crash[8]. The effects of the GFC were compounded by UK wide mortgage lending practices leading up to 2007/8 that created artificially inflated house prices[9] as people were able to access houses their personal finances could not afford.

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[1] https://www.cml.org.uk/news/press-releases/gross-mortgage-lending-increases-by-12-in-2016/ & FCA PSD
[2] UK Finance Postcode Lending Data
[3] FCA Product Sales Data
[4] Ibid
[5] https://www.cml.org.uk/news/news-and-views/uk-mortgage-market-shows-strong-regional-differences/
[6] Ibid
[7] https://www.cml.org.uk/news/news-and-views/affordability-boosts-the-northern-ireland-market/
[8] https://www.statista.com/statistics/751694/average-house-price-in-the-uk-by-country/
[9] Ibid

NI felt the effects of the GFC more acutely than other UK regions leading to a house price crash that has left large numbers of people in negative equity – where they owe more on their property than their property is worth. 25,000 households in NI remain in negative equity. The average negative equity balance is £32,000[10].

1.4 According to the then Department for Social Development (DSD, now DfC), the housing bubble of the mid-2000's particularly affected Northern Ireland, with almost 60%[11] of households considered mortgage prisoners[12], or facing affordability problems. The term mortgage prisoners was used to refer to those in negative equity, with poor credit history, fragile employment, or with interest-only loans.

1.5 The FCA have conducted a Mortgage Market Study (MMS) into the UK mortgage market with the focus of ensuring that competition in the mortgage sector is healthy and working to the benefit of consumers[13]. The MMS detailed that the mortgage market was working well in many respects, however, there was a proportion of customers who paid and continue to pay more than they need to for their mortgage. Findings also highlighted limitations to the effectiveness of the tools available to help consumers choose a cheaper mortgage, they also highlighted longstanding borrowers on high reversion rates who do not, or are unable to, switch[14].

1.6 Remedies have been agreed by the FCA and have detailed they are looking to address issues through collaboration with industry in the first instance, rather than through rule changes and will provide updates on remedies.

1.7 The Department for Communities (DfC) has developed a strategy to mitigate issues arising from negative equity. This strategy is explored in more detail in this paper. It is

[10] https://www.cml.org.uk/news/news-and-views/affordability-boosts-the-northern-ireland-market/

[11] http://www.bbc.co.uk/democracylive/northern-ireland-31438844

[12] The Financial Conduct Authority has defined mortgage prisoners as consumers who have missed out on cheaper deals that are suitable for their mortgage needs. Those on a relatively high reversion rate (the interest rate payable once an introductory rate ends), who are up to date with their payments but unable to switch. For many this is due to changes in affordability requirements following the financial crisis. - https://www.fca.org.uk/publication/market-studies/ms16-2-3-final-report.pdf (paragraph 1.3)

[13] https://www.fca.org.uk/publication/market-studies/ms16-02-1.pdf

[14] https://www.fca.org.uk/publications/market-studies/mortgages-market-study

likely that a similar strategy will be needed for the emerging mortgage issues in NI. Of most note are the numbers of people who face repossession because they do not have the option of an interest-only mortgage repayment scheme[15] or are financially unprepared for interest rate rises, having never previously experienced these[16].

1.8 The purpose of this research is to highlight distinct issues that are arising in the NI mortgage market. The research explores the root cause of these distinct issues with a view to informing workable solutions. From the research outlined in this paper, The Consumer Council believes steps need to be taken to mitigate the legacy issues highlighted:

1.8.1 Organisations with the ability to inform consumers, such as The Consumer Council, need to inform NI consumers on available options if they are in mortgage arrears, a mortgage prisoner or on an interest-only mortgage. Further work also needs to be done in NI to warn consumers of the effect an interest rise will have on their personal finances; and

1.8.2 There is evidence to suggest affordability was more stretched in NI during the GFC than any other UK region. Going forward, it is important that regulators and policymakers are confident that NI consumers are taking out affordable mortgages, even in a different interest rate environment. Therefore, The Consumer Council will be requesting the FCA are taking proportional steps to ensure high standards of new mortgage lending in NI.

1.7 The suggested mitigating actions above are explored in greater detail in the 'Recommendations' section of this paper.

[15] https://www.fca.org.uk/publication/research/fca-interest-only-mortgage-review.pdf
[16] https://www.fca.org.uk/publications/thematic-reviews/financially-vulnerable-customers-key-findings

## 2. Methodology

### Aim

2.1 The purpose of this research is to highlight distinct issues that are arising in the NI residential mortgage market. The research explores the root cause of these issues with a view to informing workable solutions.

### Scope

2.2 The research considered issues that occurred in the acquiring and holding of residential mortgages ie loans held by individuals to purchase a property for the purpose of living in. Buy to let (BTL) mortgages did not come under this scope. This is because we have treated BTL as an investment product and it was not the intention to review consumer investments. Mortgages held by businesses have also not been considered.

2.3 The research is intended to provide a snapshot of the issues that exist in the NI mortgage market at the time of writing the paper (Q2 and Q3 2017). There is no intention for this to be a regular assessment.

### Method

2.4 Where possible the research has sought to determine if a bespoke approach to NI needs to be considered by benchmarking NI to other regions within the UK.

2.5 The research has considered historical and current issues that have affected the UK mortgage market and has sought to identify how NI has been affected. Furthermore, where issues were identified we sought to ascertain whether a body holds a mitigating strategy. It has been highlighted in the text where no mitigating strategy appears to be in place by the UK government, NI Assembly or financial regulator, the FCA.

2.6 The research has primarily used secondary research sources. The research sought the views of many organisations in the course of the work. The seeking of views has come in the form of data requests and where possible meetings with organisations that operate in the NI mortgage market. These meetings were not meant to be recorded opinions but an opportunity for organisations to give their views of the market they operate within. Where views have been expressed, the research has sought data to verify.

2.7 No view expressed to The Consumer Council in the course of the research has been included in the final report. This has been to maintain the neutrality of the work and to avoid conjecture being considered as fact. Recorded conversations had the potential to discourage individuals from providing possibly useful research to protect the interests of the organisation they represented. The only views recorded in the final work are taken from secondary research sources.

# 3. Structure of the NI Mortgage Market

3.1 The structure of the market in this research refers to mortgage suppliers and how mortgages are sold. Financial services in NI are structured differently from GB in many ways. There are four dominant banks in NI financial services that either do not operate in GB, or have a much smaller presence in the GB market.

3.2 Danske Bank, First Trust (part of the AIB group), Ulster Bank (part of the RBS group) and Bank of Ireland hold 65% of the NI personal current account (PCA) market[17] and 27% of the NI mortgage market (by outstanding loans). Progressive Building Society also only operates in NI and accounts for over 7% of the NI mortgage market (by outstanding loans)[18]. Total outstanding mortgage lending in NI as at Q2 2017 is £20.7bn. Total outstanding lending as at Q2 2017 in the UK as a whole is £954.5bn[19].

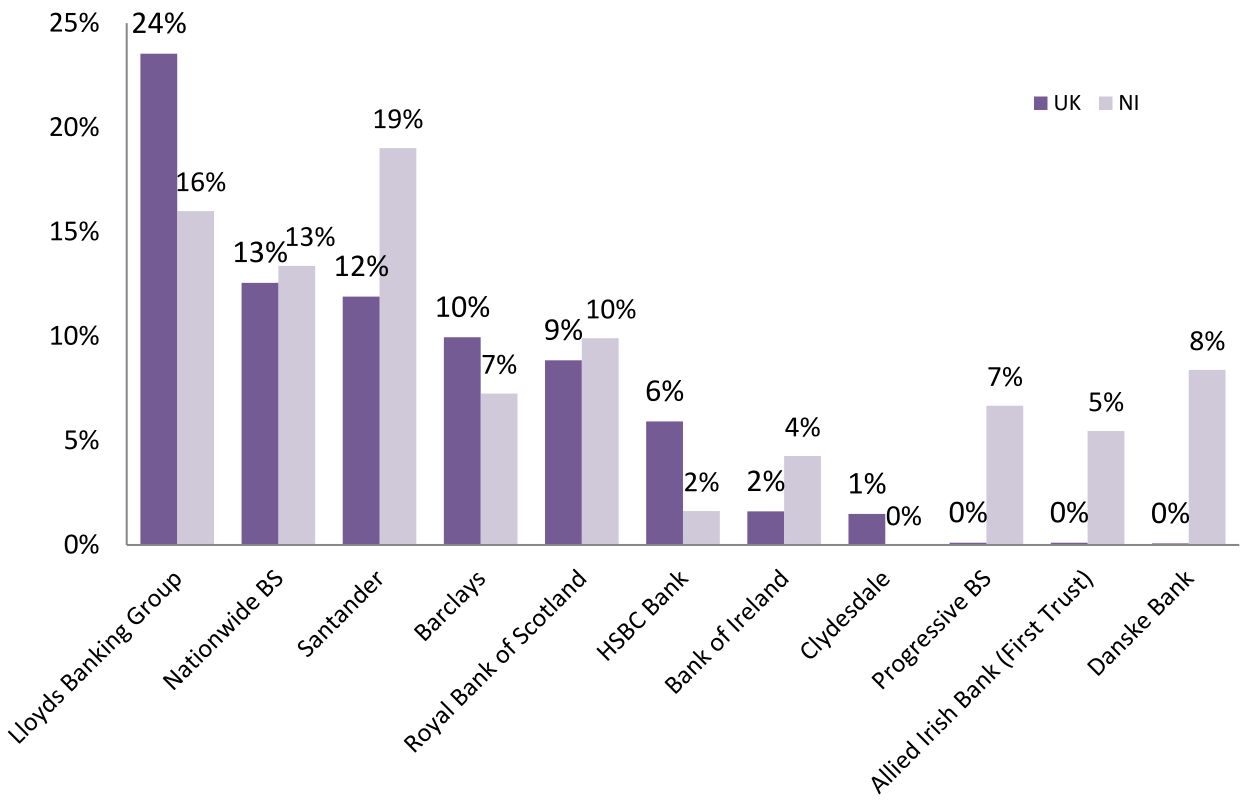
3.3 The structure of the NI mortgage market is more closely aligned to that of GB than other financial services markets in NI such as the PCA market. 75% of the NI mortgage market is held by big UK retail banks (Lloyds Banking Group (LBG), Nationwide, Santander, Barclays, RBS group and HSBC). Chart 1 shows the 2015 market share of the NI mortgage market compared to GB (in the chart, Ulster Bank's market share is included within the RBS Group figure).

3.4 There are both similarities and differences in the NI and GB mortgage market. The suppliers of mortgages in NI bears greater similarity to GB than the PCA market does in NI. The similarity in the suppliers of mortgages is from both NI & GB mortgage markets being 'intermediary led' (ie the transaction has been brokered by an Independent Financial Advisor (IFA)) rather than 'branch led' as PCAs typically are. 70% of NI's mortgages are sold through intermediaries. This is similar to the overall UK figure, where 67% of mortgages are sold through intermediaries[20]. This makes it possible for lenders who do not have a branch presence to compete in the market by

[17] https://publications.parliament.uk/pa/cm201314/cmselect/cmniaf/uc650-ix/uc65001.htm
[18] UK Finance Postcode Lending Data
[19] https://www.ukfinance.org.uk/statistics/postcode-lending/
[20] http://www.imla.org.uk/resources/imla-changing-face-of-mortgage-distribution-december-2015.pdf

offering products through third parties. Consumers are also more likely to shop around for a mortgage than they are for a bank account, which again makes it easier for new entrants to compete.

**Chart 1: 2015 NI and UK mortgage market share by outstanding loan amounts[21]**




3.5 Whilst many of the largest UK banks have a large section of the NI mortgage market, a significant proportion of the market is held by lenders who have no presence in GB. 20% of the market is held by Progressive Building Society, First Trust Bank and Danske Bank who have little or no presence in the GB mortgage market[22].

3.6 The NI mortgage market is competitive. There are sufficient numbers of active lenders in NI that mortgage rates reached record lows in 2017, alongside other UK regions[23].

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[21] UK Finance Postcode Lending Data
[22] Ibid
[23] https://www.telegraph.co.uk/business/2017/08/23/first-time-buyers-snap-properties-affordable-scotland-wales/

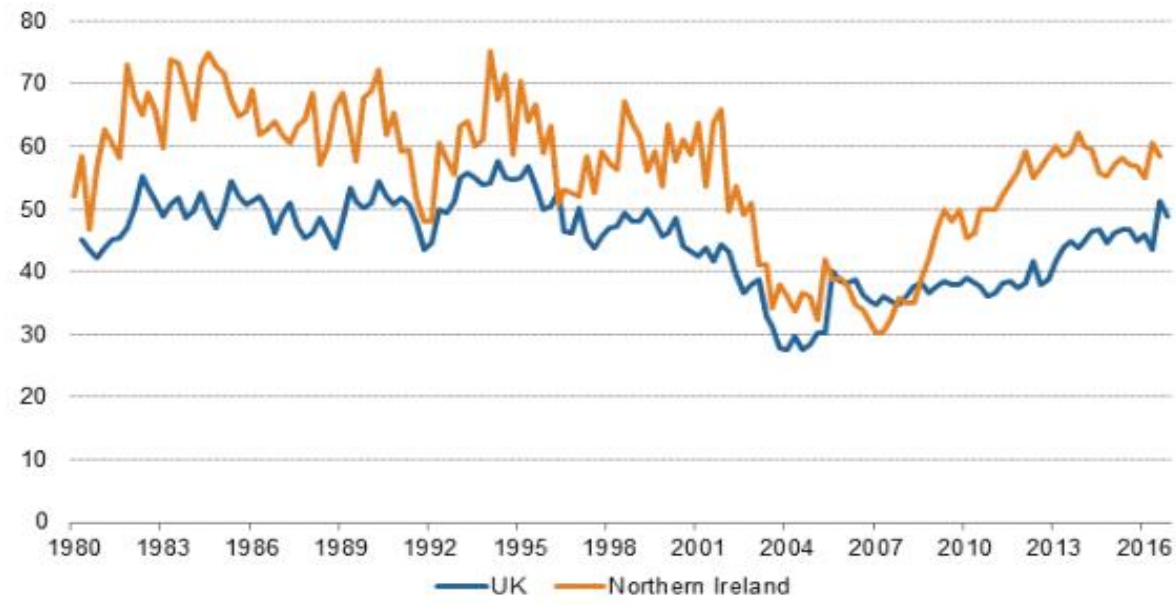
3.7 The primary concern is that the NI market is being under-monitored by UK regulators. This is due to several factors, notably its distance from London-based financial services regulators and the fact that 20% of the NI market is held by firms which, due to their relatively small size (compared to the UK) will likely receive less regulatory scrutiny.

# 4. Standard of New Mortgage Lending

### First Time Buyers

4.1 First time buyers have historically driven the NI housing market in a more significant way than in the rest of the UK. This trend dipped during the period leading up to the GFC as house prices rose, but has recovered in the eight years since the beginning of the 2008 GFC:

**Chart 2: 1980-2016 first-time buyers' % share of regulated house purchases**[24]




4.2 The outlook for NI first time buyers is positive. In 2016, they had a lower average LTI ratio than the UK as a whole (2.9 in NI compared to 3.51 in the UK). The percentage of monthly income servicing capital and interest repayments is also lower (16.2% in NI compared to 18% in the UK)[25].

4.3 Whilst the loan-to-value (LTV) ratio is slightly higher than the UK average (85.9% in NI compared to 84.3% in the UK), the difference is not significant. LTV acts as an indicator of exposure to the possibility of future negative equity in the event of a house price collapse. NI experienced high levels of negative equity as a result of the 2008 GFC. The

[24] https://www.cml.org.uk/news/news-and-views/affordability-boosts-the-northern-ireland-market/
[25] https://www.cml.org.uk/news/news-and-views/uk-mortgage-market-shows-strong-regional-differences/

current LTV of first time buyers in NI does not suggest they are at any more risk of falling into negative equity than the rest of the UK. UK Finance (formerly the Council of Mortgage Lenders (CML)) data shows how NI first time buyers compare to GB.

**Chart 3: First-time buyer affordability measures – 2016**[26]

| Region | Average Loan Size | Average Household Income | Income Multiple | Loan-to-Value | % of gross monthly household income to service capital and interest repayments |
|---|---|---|---|---|---|
| **Greater London** | £258,400 | £64,500 | 3.98 | 75.2% | 18.9% |
| **Scotland** | £99,800 | £33,600 | 3.03 | 85.0% | 16.6% |
| **Wales** | £108,000 | £33,800 | 3.31 | 86.1% | 17.2% |
| **Northern Ireland** | £91,400 | £31,500 | 2.9 | 85.9% | 16.2% |
| **UK** | £132,800 | £40,000 | 3.51 | 84.3% | 18.0% |

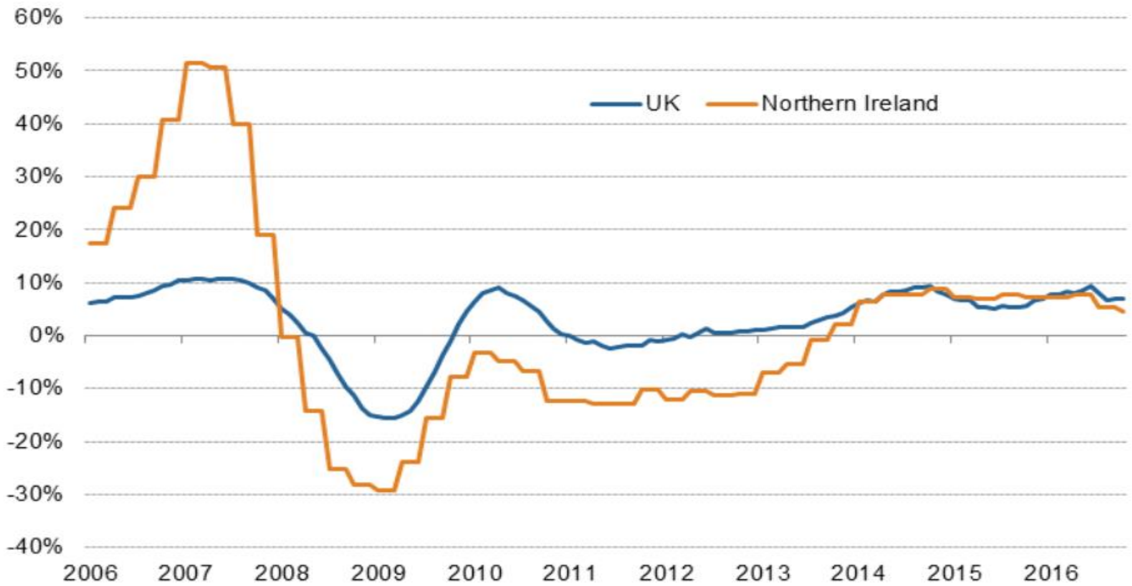
### Overall Mortgage Population

4.4 The picture for the last 12 months is similar. The February 2017 Halifax Affordability Review[27] shows that of 12 UK regions, NI has the second lowest level of mortgage payments as a percentage of disposable income in Q4 2016 for first time buyers. However, this has not always been the case. In 2007, NI had the highest level of mortgage payments as a percentage of monthly income compared to any region in the UK for first time buyers (63.5% compared to a UK average of 47.7%). This suggests a significantly improving picture for new buyers in NI. The 2008 GFC particularly affected the NI housing market. House prices across the UK fell, but in NI house prices crashed (Chart 4).

4.5 NI house prices fell each year between 2007 and 2013. 2014 research undertaken by Homeloan Management Limited (HML)[28] found that by the end of 2013, 68,000 homeowners (41% of borrowers) were in negative equity[29].

[26] https://www.cml.org.uk/news/news-and-views/uk-mortgage-market-shows-strong-regional-differences/
[27] http://static.halifax.co.uk/assets/pdf/mortgages/pdf/halifax-mortgage-affordability-2-feb-2017-housing-release.pdf
[28] https://www.housingrights.co.uk/news/41-northern-ireland-homeowners-trapped-negative-equity
[29] http://www.bbc.co.uk/news/business-26389009

**Chart 4: House price changes as % change from previous year, NI and UK**




Source: Land & Property Services/ NISRA

4.6 Appendix 1 presents NI house prices against the UK average. It shows that after many years of falling house prices, growth in NI house prices are coming into line with the rest of the UK. Small, steady growth of house prices is needed in securing the long term financial positions of those taking out mortgages at the moment. As home owners in NI will know only too well, house prices can go down as well as up. The need to maintain sustainable lending is therefore imperative.

4.7 Whilst there are some positive indicators around the standards of new mortgage lending in NI, there are some concerns to note. These include the possibility that new lending in NI may be subject to less regulatory scrutiny from the likes of the FCA than other parts of the UK. This is because there are several firms that only lend in NI. Such firms account for at least 20% of the NI mortgage market[30]. Due to these firms' small share of the total UK market, it is unlikely they would receive much attention from UK financial regulators; however, regionally their impact is significant. The second concern is that all financial regulatory bodies are led from London and there is no NI

[30] UK Finance Postcode Lending Data

regional representation to these bodies. This means that specific NI issues will be difficult to consider.

4.8 A further concern is evidence that NI is in a consumer credit-driven economic bubble (even more so than the rest of the UK). Whilst not the focus of this work, the increasing level of unsecured debt will eventually effect people's ability to repay their mortgage, particularly if interest rates rise. Total gross consumer lending excluding student loans in the UK has risen 15.1% in two years (from March 2015 to April 2017)[31]. The Money Advice Service (MAS) found that NI had the highest level of overall indebtedness of any UK region[32]. The debt charity StepChange found that their NI clients had the highest debt to income ratio (94% compared to a UK average of 82%)[33]. If this credit bubble bursts it will inevitably have an impact on people's ability to repay their mortgage. For this reason the outlook for new lending must be cautiously optimistic.

[31] https://www.statista.com/statistics/311415/uk-lending-total-gross-consumer-lending-in-the-united-kingdom/
[32] https://masassets.blob.core.windows.net/cms/files/000/000/337/original/MAS_Report_10.03.2016.pdf
[33] https://www.stepchange.org/Portals/0/documents/media/Scotland_in_the_Red.pdf

# 5. Legacy Issues

5.1 ‘Legacy issues’ are created in the mortgage market when an economic event, change in personal circumstances or specific lending practice creates a problem for the home owner with a mortgage that continues to exist long after the event has taken place. When the legacy issue arises as a result of a widespread lending practice or a macro-economic event, the numbers of those affected can be significant. When legacy issues become widespread, relevant regulatory and governmental authorities often develop a regional or national strategy to minimise their effect. A national strategy is already in place for many mortgage legacy issues, such as interest-only mortgage maturity.

5.2 As stated, The Consumer Council is assessing whether NI is disproportionately affected by specific financial services issues. To that end, we have assessed if the NI mortgage market is more affected by any particular legacy issue compared to GB. We have assessed NI exposure to the following UK wide legacy issues:

- Endowment mortgages;
- Interest-only mortgages;
- Negative equity; and
- Trapped borrowers (‘Mortgage Prisoners’).

### Endowment mortgages

5.3 In the 1980s and 1990s, endowment linked mortgages were more popular than traditional repayment mortgages. In 1988, 83% of new mortgages were endowment linked[34]. Even by mid-2000, 23% of new mortgages were still endowment based.

5.4 In theory, endowment mortgages made sense. A house buyer would hold an interest-only mortgage with one lender and then take out an investment (ie an endowment policy) with an insurer. This investment, upon maturity, would provide sufficient return to repay the mortgage. Many holders of endowment policies were promised

[34] http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN00570#fullreport

that not only would their mortgage be repaid but their investment return would exceed the value of their remaining mortgage.

5.5 The problem was that the figures used to project investment returns were from the late 1970s, when inflation reached peaks of 24%. So even when investments were making small real term (post inflation) gains, the actual returns for an endowment investment could be up to 20% in a year. However, by the 1990s inflation - and therefore actual returns on investment - was much lower. From 1982 inflation was never higher than 10% and never higher than 5% after 1991[35].

5.6 As it became apparent that these policies were not going to reach their promised values, many customers tried to make compensation claims against their investment provider (usually an insurance company). By 2006, £2.2bn had been paid out to people who were mis-sold endowment mortgages[36].

5.7 Whilst endowment mortgages were a previously large mis-selling issue, not much can be done now for those whose endowment policy has matured recently, or is about to mature, at a much lower value than expected. This is because of FCA and Financial Ombudsman Service (FOS) rules on claiming compensation on mis-sold endowment policies. FCA rules state:

> *'(1) If a complaint relates to the sale of an endowment policy for the purpose of achieving capital repayment of a mortgage and the complainant receives a letter from a firm or a VJ participant warning that there is a high risk that the policy will not, at maturity, produce a sum large enough to repay the target amount then, subject to (2), (3), (4) and (5):*
>
> *(a) time for referring a complaint to the Financial Ombudsman Service starts to run from the date the complainant receives the letter; and*

[35] http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN00570#fullreport
[36] http://www.independent.co.uk/news/business/news/mortgage-banks-count-the-cost-of-endowment-mis-selling-and-cuts-5329938.html

*(b) ends three years from that date ("the final date").'*[37]

5.8 This means that people have three years, from being informed by their endowment provider that their policy is likely to have lower than expected returns, to make a compensation claim. The vast majority (if not all) of endowment providers informed their customers of this lower than expected return more than three years ago.

5.9 FCA data on interest-only mortgages suggests that NI has sold a lower proportional number of endowment policies than other parts of the UK. This is because those with endowment policies may be expected to have taken out an accompanying interest-only mortgage. NI has fewer interest-only mortgages than the rest of the UK.

5.10 Therefore there would be little point in The Consumer Council undertaking work now to advise NI customers of possible compensation available on mis-sold endowment policies, given not many, if any, would be eligible to make a complaint.

### Interest-only Mortgages

5.11 Possibly the biggest legacy of endowment mortgages today is the number of households who have interest-only mortgages. Currently, 1.7m people[20] in the UK have an interest-only mortgage. Many of these 1.7m people risk repossession of their home if they do not have a plan to repay their mortgage by the time their mortgage matures.

5.12 Whilst with traditional repayment mortgages an individual pays off the interest and some of the capital each month, with interest-only mortgages only the interest is repaid. Customers should use savings, investments or other assets (known as 'repayment vehicles') to pay off the total amount borrowed at the end of their mortgage term.

[37] https://www.handbook.fca.org.uk/handbook/DISP/2/8.html

5.13 Interest-only mortgages can suit many people's circumstances, provided they have the ability to repay the remaining capital at the end of the term. A common form of interest-only mortgage is an endowment policy, which is referred to above. However, if the individual does not have a suitable repayment vehicle at the end of their mortgage term then the lender could repossess the property. Interest-only mortgage customers who are not paying into a suitable repayment vehicle are also more likely to fall into negative equity in the event of a housing market downturn as they have not been increasing the equity in their property.

5.14 Many people will take on an interest-only mortgage at the point of acquiring a mortgage, while others convert part way through. Whilst not always the case, conversion to an interest-only mortgage can be a sign of financial distress as individuals look for ways to reduce their monthly outgoings.

5.15 Interest-only mortgages were previously widely sold across the UK. By the late 1980s, 80% of all mortgages taken out were interest-only[38]. This was largely due to the popularity of endowment mortgages. By 2012, the sale of interest-only mortgages was down to just 10% of all mortgages sold in the UK and only 2% of first time buyers[39].

5.16 However, the legacy of interest-only mortgages remains. By December 2011, 29.4% of all UK regulated residential mortgages (2.6 million of 9 million) were interest-only[40]. Of these 2.6 million mortgages, 80.3% were sold on interest-only terms, while 19.7% were converted to an interest-only mortgage part way through the mortgage term[41]. There was some concern following the 2008 GFC that many of the 2.6m interest-only customers in the UK did not have a suitable repayment strategy. In 2013, the FCA conducted a review into the UK's interest-only mortgage market and drew the following conclusions[42]:

[38] https://www.cml.org.uk/news/news-and-views/469/
[39] Ibid
[40] https://www.fca.org.uk/publication/research/fca-interest-only-mortgage-review.pdf
[41] Ibid
[42] https://www.fca.org.uk/news/press-releases/fca-publishes-findings-review-interest-only-mortgages-and-reaches-agreement

- *'10% of people did not have a strategy to repay their interest-only mortgage.*
- *37% believed they may not have enough money to pay off the loan, while the FCA's own research suggested it was closer to 48%.*
- *Borrowers who were able to give a figure believed their shortfall would be, on average, £22,100. However, according to FCA estimates, approximately half of these shortfalls are expected to be over £50,000.*
- *The vast majority of interest-only borrowers (81%) said they understood the terms of the loan at the point of sale. But 13% said they did not; 6% were unsure.*
- *While most borrowers (70%) check their annual mortgage statement to ensure they are on track to repay at maturity, 14% never check.*
- *The average outstanding balance of an interest-only mortgage customer is £55,000 for those with an 'endowment mortgage' (ie one that was sold backed by an endowment policy), and £121,000 for those without.'*

5.17 The FCA's research points to a difference between the number of people who said they have a repayment strategy and the number with a realistic repayment strategy. Therefore the number of people without a realistic repayment strategy to their interest-only mortgage is likely to be much higher than 10%. Many interest-only customers will have a realistic repayment strategy, however a significant number of people do not. Over the next 25 years as these mortgages mature, many people could lose their home as they do not have a suitable repayment vehicle.

5.18 The FCA's research also found that the NI market had two significant points of difference to the overall UK market. While it had fewer interest-only mortgages as a percentage of total mortgages sold than other parts of the UK, the NI market had a much higher proportion of mortgage customers converting to interest-only mortgages. The table below shows how NI compares to other UK regions with regard to the purchase and conversion to interest-only mortgages[43]:

**Chart 5: 2013 Index of Interest-only % of Total Residential Mortgage Stock**


*Total number of interest-only mortgages as % variance from UK average*
*Total number of interest-only mortgages sold initially as interest-only as % variance from UK average*
*Total number of interest-only mortgages converted to interest-only mortgage as % variance from UK average*

***Source:*** *Equifax (cited in FCA's Interest-only Mortgage Review)*

5.19 There are different ways to interpret NI's exposure to the interest-only mortgage market. The first is that NI has a more 'traditional' financial services market (ie that new and 'innovative' financial services products gets less uptake in NI). This view is backed up by Office for National Statistics (ONS) research that shows NI has significantly lower uptake of more 'innovative' savings products such as ISAs, share

[43] https://www.fca.org.uk/publication/research/fca-interest-only-mortgage-review.pdf

holdings, unit trusts, Premium Bonds and National Savings Bonds than the rest of the UK[44]. This is noteworthy in that NI may be shielded from future mis-selling issues or that people in NI could miss out on products that could improve their personal finances.

5.20 The second interpretation of the data is to note that NI has significantly higher levels of conversion to interest-only mortgages than other UK regions. As stated earlier, interest-only conversion can be a sign of financial distress. The timing of the research in 2013, five years after the 2008 GFC, shows in part how NI was affected by this occurrence.

5.21 It is important to draw a distinction between financial distress caused by poor affordability checks prior to the 2008 NI house price collapse and the resulting widespread negative equity experienced. Monthly payments for instance, do not fluctuate with house prices. As stated earlier in this report, in 2007, the average new NI mortgage to first time buyers accounted for 63.5% of total income. It is not surprising, therefore, that many people in NI opted to switch to interest-only mortgages in the years that followed. Chart 6 below shows that in 2016, homeowners in NI continue to have higher levels of mortgage arrears, again a warning of overall financial distress.

5.22 Following the FCA's 2013 research into the interest-only mortgage market, the number of people UK wide on an interest-only mortgage fell from 2.6m to 1.7m in 2016 as mortgages have come to the end of term. Mortgage firms have sent letters to 980,000 customers with interest-only mortgages maturing prior to 2020, to inform them of their mortgage repayment position and provide them with the opportunity to act if necessary.

[44] https://www.gov.uk/government/collections/family-resources-survey--2

**Chart 6: Q2 2016 Mortgage Payment Shortfalls by Region (for all mortgage types)[45]**

| Post Code Region | Payment Shortfall Rate |
|---|---|
| Eastern | 2.50% |
| East Midlands | 3.20% |
| Central & Greater London | 2.90% |
| North East | 4.50% |
| Northern Ireland | 6.00% |
| North West | 4.30% |
| Scotland | 3.40% |
| South East | 2.50% |
| South West | 2.30% |
| Wales | 4.40% |
| West Midlands | 3.80% |
| Yorkshire and The Humber | 4.00% |
| **Grand Total** | **3.40%** |

5.23 The primary issue, from a consumer protection perspective, is that customers need to engage years ahead of their mortgage term finishing, or risk losing their home. As noted above, there is a national strategy in place to support interest-only mortgage customers to develop a repayment strategy. The national strategy appears to be proving effective as the number of people on interest-only mortgages is falling.

5.24 The Consumer Council will look to provide information to vulnerable consumers who may not be actively engaging with their lender. The Consumer Council is committed to increasing the awareness of the need for a repayment strategy amongst home owners with an interest-only mortgage. The provision of this information by an independent organisation (ie not the lender) can sometimes be more compelling and persuasive.

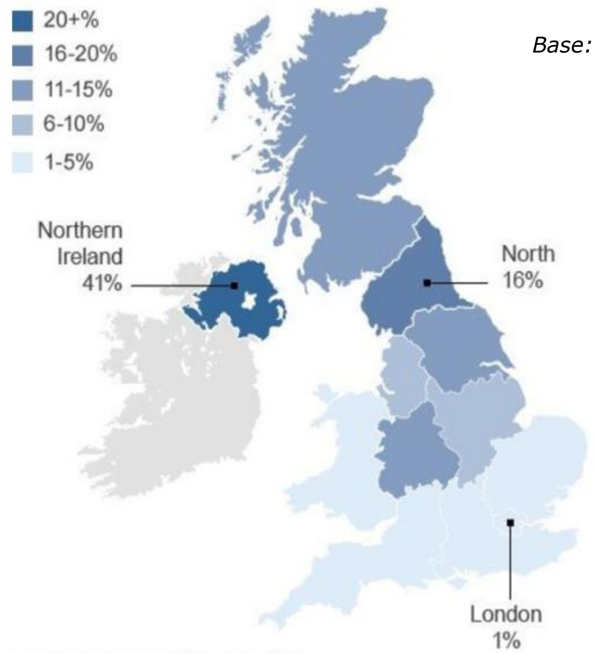
[45] FCA Product Sales Data – Q2 2017

## Negative Equity

5.25 The level of negative equity in NI in the last decade is well documented. In the context of the mortgage market, negative equity occurs when the current price of the property does not cover the remaining balance on the mortgage. When in negative equity, even if the property is sold, the customer will still owe money to the lender. For many people, being in negative equity means they are unable to sell their property. This is particularly problematic if the individual in question has stretched their affordability to get the mortgage in the first place. It also means that some people are unable to sell a house they cannot afford to live in.

5.26 Chart 4 demonstrates the volatility in house prices in NI in the 11 years to 2017. 50% growth followed by six years of house price falls left a generation of home owners in negative equity. By the end of 2013, 41% of borrowers in NI who took out a mortgage between 2005 and 2013, (the equivalent of 68,000 homeowners) were in negative equity[46]. Whilst other areas of the UK also experienced house price falls in this time, NI was significantly more affected than other areas as illustrated in Chart 7:

**Chart 7: UK Negative Equity Map 2013 – Percentage of Borrowers in Negative Equity[47]**




*Base: mortgages advanced since 2005*

*Source: HomeLoan Management Limited (HML)*

[46] http://www.bbc.co.uk/news/business-26389009
[47] Ibid

5.27 Since 2013, NI house prices have started to rise again. UK Finance estimate that by mid-2016 the number of people in NI in negative equity had fallen from 68,000 to 25,000. This still means however, that 10% of the total number of home owners with a mortgage in NI are in negative equity. UK Finance estimates the average negative equity balance is £32,000[48]. The situation in NI therefore, whilst improving, remains critical. Given the high levels of negative equity and arrears it is not surprising that NI continues to have the highest repossession rates in the UK:

**Chart 8 – UK Residential Property Repossession Rate Forecast 2015[49]**

| Region | Repossession Rate Forecast | Total Forecast Repossessions |
|---|---|---|
| East of England | 0.17% | 1,742 |
| East Midlands | 0.13% | 1,027 |
| Greater London | 0.25% | 2,641 |
| North | 0.23% | 1,045 |
| North West | 0.17% | 2,153 |
| **Northern Ireland** | **0.49%** | **1,571** |
| Scotland | 0.16% | 1,729 |
| South East | 0.17% | 2,605 |
| South West | 0.14% | 1,222 |
| Wales | 0.26% | 1,354 |
| West Midlands | 0.23% | 2,082 |
| Yorkshire & Humber | 0.16% | 1,435 |
| Total UK | 0.20% | 20,606 |

*Source: HML*

5.28 DfC has developed a strategy to mitigate the impact of negative equity[50]. In 2014, the then Department for Social Development (DSD) issued a report and made the following recommendations:

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48 https://www.cml.org.uk/news/news-and-views/affordability-boosts-the-northern-ireland-market/
49 HML Forecast in 2014 for 2015.
50 https://www.communities-ni.gov.uk/topics/housing/housing-repossessions-taskforce

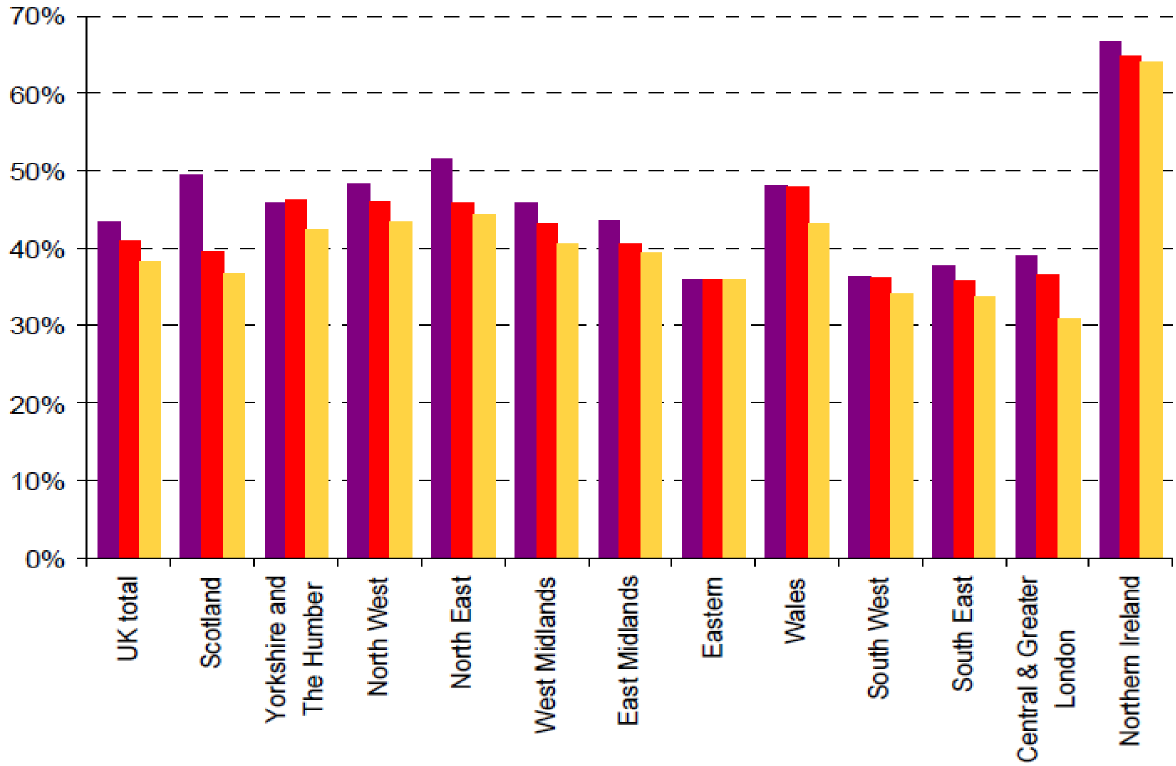
- *'the establishment of a 'mortgage options hub' for the delivery of specialist mortgage debt advice at an early stage;*
- *borrowers take responsibility for improving their debt position by accessing the free and independent channels of advice that suit their needs;*
- *working with the behavioural insights team to examine how behavioural economics can provide an innovative stimulus to borrower engagement;*
- *a review into the way in which lenders communicate voluntary exits, including assisted voluntary sale schemes, to their customers;*
- *commissioning the Northern Ireland Federation of Housing Associations to complete a feasibility study on the potential of a mortgage rescue scheme in Northern Ireland;*
- *timely assistance from the Northern Ireland Housing Executive, including a homelessness assessment for vulnerable households.'*

5.29 Given the comprehensiveness and currency of the DSD (now DfC) report, The Consumer Council does not recommend further research in this area. The Consumer Council will draw the attention of stakeholders to the DfC strategy for addressing the potential consequences of negative equity.

### Trapped Borrowers ('Mortgage Prisoners')

5.30 A further and separate issue is that many NI borrowers have become 'mortgage prisoners'. This is when people are trapped in mortgage deals that met pre 2008 affordability requirements, but not those introduced by the FCA and its predecessor organisation, the Financial Services Authority (FSA) post the 2008 GFC. Distressed customers who need to lower their monthly repayments are unable to take advantage of the lowest interest rates available. This means they are neither able to change mortgage nor move house. According to the FSA, as many as 65% of NI's home owners with a mortgage were 'mortgage prisoners' in 2012, the highest number anywhere in the UK:

**Chart 9 – 'Mortgage prisoners' by region 2012**[51]




***Source:*** *FSA Product Sales Data Performance data 2012, Acadametrics, Halifax, Nationwide and FSA estimate*



5.31 Chart 9 shows that while 65% of home owners in NI with a mortgage were mortgage prisoners, this was the case for only around 40% in the UK. By 2015, the situation was only marginally better. According to the DSD, 'just under 60%' of NI home owners with a mortgage were mortgage prisoners[52].

5.32 It is imperative that consumer bodies such as The Consumer Council encourage home owners with a mortgage to engage with the issue at the earliest possible stage. Some customers may treat their lenders with suspicion, but most lenders will have an established and robust policy to assist trapped borrowers. Given the levels of overall indebtedness that exists across the UK, but especially in NI, it is highly likely that many 'mortgage prisoners' will have other unsecured debts. The Consumer Council will therefore work to encourage consumers to seek specialist debt advice.

[51] https://www.fca.org.uk/publication/archive/fsa-mmr-datapack2012.pdf
[52] http://www.bbc.co.uk/democracylive/northern-ireland-31438844

### Mortgage Rescue Scheme

5.33 One option that has been discussed at some length is an NI 'mortgage rescue scheme'. The NI Assembly recommended a rescue scheme back in 2008[53]. Such a scheme could offer assistance to those who cannot find solutions in the marketplace. After a consultation process no scheme materialised. Between, 2008-2011, DSD ministers bid for funds to launch a financial rescue element, without success[54].

5.34 In June 2011 the DSD Minister stated they *"support the ideals of a mortgage rescue scheme for Northern Ireland",* but that a full scheme could cost £8.25 million over a two-year period and might only enable 72 'rescues'[55]. The scheme would also impact on other budgets (eg health). In 2012 the 'mortgage rescue scheme' was rejected by the then NI Housing Minister after DSD said a local scheme would not help enough people[56].

5.35 In 2015, the DSD called for the Northern Ireland Federation of Housing Associations (NIFHA) to undertake a further feasibility study regarding a potential mortgage rescue scheme in NI with findings to be reported in spring 2015[57]. Following this feasibility study, it was again decided that a mortgage rescue scheme in NI was not viable[58].

5.36 Whilst a mortgage rescue scheme could have helped many people post GFC, it has been nearly 10 years since the first effects of the GFC were seen in the NI housing market. Multiple attempts at a rescue scheme have been proposed but for different reasons were not deemed viable. Given this, it is not likely that one will be introduced in the foreseeable future. Consumers will need to look to options available in the market place. Options do exist that can assist either those in negative equity or are a mortgage prisoner but consumers may need signposting to them.

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[53] http://archive.niassembly.gov.uk/io/research/2008/10808.pdf
[54] http://slideplayer.com/slide/1468963/ - NIHE
[55] Ibid
[56] http://www.bbc.co.uk/news/uk-northern-ireland-17250424
[57] https://www.communities-ni.gov.uk/sites/default/files/publications/dsd/housing-repossessions-taskforce-final-report.pdf
[58] *Feasibility Report seen. Provided by NIFHA - not in the public domain*

# 6. Emerging Issues

6.1 It is important to assess issues that could affect the NI mortgage market in the years ahead. Our research is not exhaustive, but we have tried to assess some of the most pressing issues within an NI context:

**The Rise of Interest Rates**

6.2 In March 2009, in the aftermath of the effects of the 2008 GFC, the Bank of England cut interest rates to 0.5%. Different commentators had different views as to how long interest rates would remain this low. Not many would have predicted that eight years on, interest rates would be even lower. Interest rates were in part lowered to bolster consumer spending. This was achieved; however, in April 2017, the Bank of England warned that a growing consumer credit bubble had the potential to damage banking stability[59]. Whilst some consumers have used the low interest rate environment to repair their financial position, many have chosen to make the most of cheap credit and increased their spending. As at February 2017, credit card debt had grown at its fastest pace in 11 years, to a new high of £67.3bn across the UK[26].

6.3 One of the unintended consequences of record low interest rates is that a whole generation of home owners with a mortgage have never experienced anything other than low interest rates. In 2015, the Money Advice Trust charity claimed more than one million people had never experienced an interest rate rise on their mortgage[60]. This figure is rising each year the base rate interest rate does not rise. The buoyancy of the NI first time buyer market leaves NI more exposed to the eventual rise in interest rates.

6.4 The FCA conducted research in late 2016 into how prepared lenders and home owners with a mortgage were for the effects of interest rate rises[61]. UK Finance has provided

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[59] http://www.telegraph.co.uk/business/2017/04/04/risky-lending-will-endanger-banks-credit-bubble-bursts-bank/
[60] http://www.bbc.co.uk/news/business-33786528
[61] https://www.fca.org.uk/publications/thematic-reviews/financially-vulnerable-customers-key-findings

the following example of what might happen to different mortgage customers in the event of an interest rate rise:

**Chart 10: How a 0.25 % rise in base rates 'might'[62] affect a mortgage[63]**

| Loan Size | Existing Monthly Repayment | Increase after 0.25% Rise |
|---|---|---|
| **£50,000** | £283 | +£7 |
| **£100,000** | £566 | +£13 |
| **£150,000** | £849 | +£20 |
| **£200,000** | £1,132 | +£26 |
| **£250,000** | £1,415 | +£33 |

*Source: UK Finance (Formerly CML)*

6.5 In isolation, a 0.25% interest rate rise appears to have a small impact on household expenditure. However, if the Bank of England base interest rate started to rise to anything close to pre-crisis levels (5.75%[64]) then the shock would be significant. Based on the above example, if an individual had a £100,000 mortgage and the base rate rose to the 2007 level of 5.75% then the monthly mortgage payment would rise by £286. Many people do not have that level of flexibility in their budget.

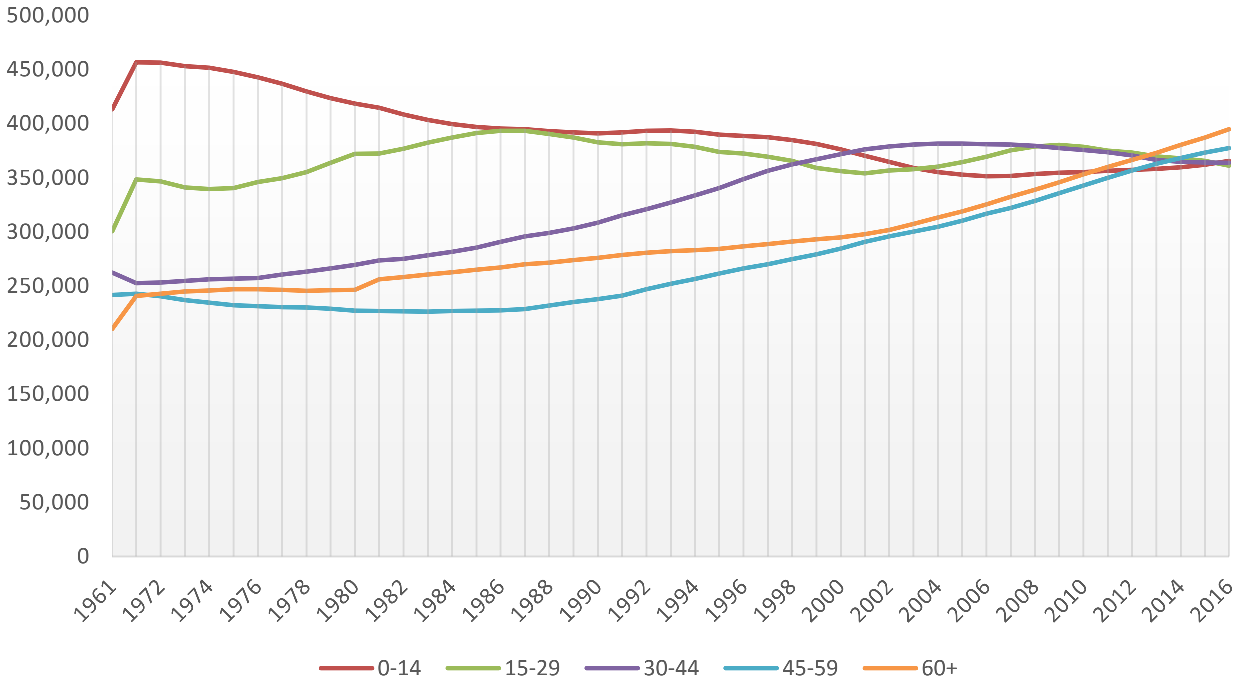
6.6 The significantly higher number of customers in arrears and deemed 'mortgage prisoners' indicates that there are many more mortgage customers in NI who are just able to pay their mortgage compared to the UK. The Consumer Council along with other independent bodies needs to work to raise awareness of the need to take into account rises in interest rates when entering into financial obligations.

[62] 'Might' is used as the example is based on the assumption of 20 year mortgage term remaining. Example is only indicative and the exact variation will depend on the mortgage terms of the individual
[63] https://www.cml.org.uk/news/news-and-views/673/
[64] 2007 Bank of England Base Interest Rate

### Ageing Population

6.7 Another challenge mortgage companies and consumers will face is how to adapt mortgage lending to an ageing population. The traditional life cycle of mortgages no longer holds true. Historically many people would have taken on a 25 year mortgage in their 20s and 30s, with the aim of having their mortgage paid off prior to retiring at 65.

**Chart 11 - Population of Northern Ireland by Age Demographic (1961-2016)** [65]




6.8 The age demographic in NI (as well as the rest of the UK) is shifting. In NI, between 1961 and 2016, the under 60 population has risen by 21%, whilst the over 60 population has risen by 81%. In the same period, the average age of UK first time buyers has risen from 23 years old[66] to 36 years old[67]. With repayment terms available on mortgages up to 40 years, many families face the prospect of still owing a substantial amount on their mortgage by the time they reach retirement age. The shift

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[65] https://www.nisra.gov.uk/publications/2016-mid-year-population-estimates-northern-ireland
[66] http://www.royalmailgroup.com/35-years-old-average-age-first-time-buyers-expect-join-housing-ladder
[67] http://www.propertywire.com/news/europe/uk-first-time-buyers-28/

in age demographics means this prospect will apply to an increasing number of households in NI.

6.9 Needing a mortgage whilst in retirement is not an issue that is exclusive to NI. It will affect the whole of the UK. As of the 2011 Census, NI had a slightly lower median age compared to the UK (37 years old in NI compared to 40 years old in the UK). However, there are factors that may cause the issue to become more significant in NI than in the UK as a whole. In a low birth rate country such as the UK, migration will be a leading factor in growing the under 60 population. NI has the lowest immigration rates in the UK[68]. NI's population is also predicted to grow at a slower rate than the UK as a whole. Between 2015 and 2035, the UK population is expected to grow by 13%, whilst the NI population is only expected to grow by 7.9%[69]. The number of people in NI aged 65 and over is expected to increase by 74.4% between 2014 and 2039[70]. An ageing population with low population growth, points towards older customers being increasingly important to mortgage lenders.

6.10 After the GFC, lending requirements tightened with the introduction of the FCA's mortgage market review (MMR). Many UK lenders became hesitant to lend to people entering retirement[71] but for many people, home ownership is not realistic unless they are able to borrow into retirement. Lenders need to adapt to a changing population. Lender's lending criteria will need to recognise pension income in the same way as income from a job.

6.11 How accessible mortgages are for those seeking a mortgage towards the end of their working life and into retirement will need to be monitored by policy makers and lenders to ensure that people are able to keep hold of their home as they enter retirement.

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[68] http://www.belfasttelegraph.co.uk/news/northern-ireland/northern-ireland-has-uks-lowest-immigration-rate-31331243.html

[69] https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/populationestimates/bulletins/annualmidyearpopulationestimates/latest

[70] http://www.ageuk.org.uk/northern-ireland/act4age/brexit/

[71] http://www.mortgagesolutions.co.uk/news/2014/11/24/lenders-fear-fca-backlash-over-lending-into-retirement/

## 7. Recommendations

7.1 This report has covered a number of different areas of the NI mortgage market. There are signs that new lending in NI is improving. In the last 10 years, NI has moved from being the least affordable place to get a mortgage (in terms of mortgage payments as a % of overall disposable income) to the second most affordable of the 12 UK regions assessed[72]. There are signs that NI is the best place in the UK to be a first time buyer. On average the LTI ratio of first time buyers is the lowest in the UK (2.9 LTI multiple, compared to a UK average of 3.51). The percentage of monthly income for first time buyers to service capital and interest repayments is also the lowest in the UK (16.2% in NI compared to 18% across the UK).

7.2 The standard of new lending only tells part of the story of the NI mortgage market. Of the 12 UK regions assessed, NI has the:

- Highest proportion of home owners with a mortgage who switched to interest-only mortgages during the term of their mortgage (most likely due to capital repayments becoming unaffordable);
- Highest proportion of home owners with a mortgage in mortgage arrears;
- Highest number of home owners in negative equity; and
- Highest proportion of home owners with a mortgage considered to be 'mortgage prisoners'.

7.3 NI needs to ensure that the standards of new mortgage lending remain high so that past mistakes will not be repeated on a new generation of borrowers. A set of bold and pragmatic solutions are needed to help alleviate many of the legacy issues

[72] http://static.halifax.co.uk/assets/pdf/mortgages/pdf/halifax-mortgage-affordability-2-feb-2017-housing-release.pdf

discussed in this paper. A consumer credit led bubble and lack of preparation for an eventual interest rate rise pose the greatest economic risk to a stable mortgage market. Furthermore, failure to adapt to the lending needs of an ageing population has the potential to lead to detriment. House prices, poor standards of lending, the failure of endowment policies and the overall economic environment are beyond the control of NI home owners with a mortgage.

7.4 However there are many options available if people choose to engage with the issue. Options include extending the term of a mortgage to make monthly payments more manageable, being placed onto an interest-only mortgage for a fixed period of time, switching mortgage rates, getting a mortgage with a specialised lender or voluntarily allowing a property to be repossessed in exchange for a reduction in the loan amount. The Consumer Council, through its widespread communication channels will work to raise awareness of this need.

7.5 The following recommendations take account of the specific role of The Consumer Council and other key stakeholders:

**Increase public awareness in NI on key mortgage issues**

7.6 More information is needed for people who have an interest-only mortgage, are a 'mortgage prisoner' or are in negative equity. Whilst lenders have made much progress in awareness raising of interest-only mortgages, further information from an independent body may assist people to take steps to address the issues.

7.7 Some 'mortgage prisoners' may still have options available to them. Crucially mortgage prisoners need to seek independent financial advice to have their options assessed and to develop a long term strategy that would increase affordability. This could include tackling other debt to increase the mortgage options available to them in the long run.

7.8 Many people in negative equity may also wrongly think they do not have options. For example, some lenders may be willing to settle the mortgage for a lower amount given the wider economic environment. Again, those affected people need to engage with the issue. The first step must be to open up communication channels with their lender to have their options assessed.

7.9 It is not proposed to produce any information on endowment policies or on the arrears process. This is because the majority of people are unable to seek compensation on their endowment policy, even if it was mis-sold. For those in arrears, it is likely their lender has informed them of their situation and the steps needed to be taken. The Consumer Council is well placed to increase awareness of other mortgage issues through its media profile and programmes that interact directly with consumers.

### Mortgage lending standards must remain high

7.10 The FCA's 2014 MMR has sought to strengthen the requirements needed to obtain a mortgage following lax lending standards leading up to the 2008 GFC[73]. In this same time period leading up to the 2008 GFC, NI's housing market became the most overheated in the UK[74] leading to a generation of NI home owners being pushed into negative equity.

7.11 The need for high standards of affordable new mortgage lending are of particular importance for NI as its housing market is still in fragile recovery and its consumers are heavily indebted. There is nothing seen in the course of this research to indicate there is an issue with current mortgage lending in NI. However it would be prudent to have the quality of lending files in NI reviewed impartially to ensure the recovery in the NI housing market is on a solid foundation.

7.12 This would need to be undertaken by the FCA, in its role as the industry's conduct regulator. The Consumer Council will therefore be asking the FCA to ensure that NI mortgage files are being assessed in future mortgage thematic reviews[75].

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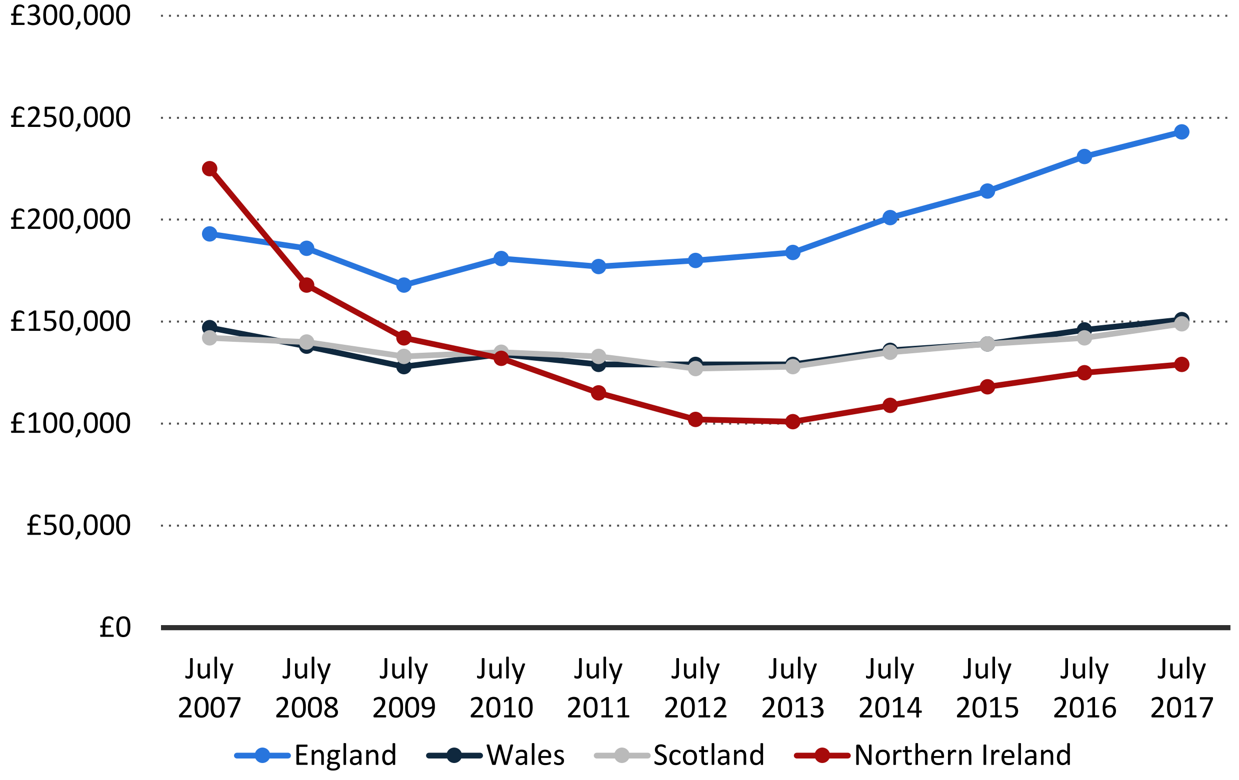
[73] https://www.mortgagestrategy.co.uk/issues/1-april-2015/cover-story-mmr-one-year-many-changes/.
[74] https://www.statista.com/statistics/751694/average-house-price-in-the-uk-by-country/
[75] https://www.fca.org.uk/about/supervision/thematic-reviews

7.13 Innovative solutions are needed to address the issues in the NI mortgage market. Without intervention, overall indebtedness stands to rise and many homes may needlessly remain in negative equity. The Consumer Council welcomes feedback and engagement from other bodies interested in discussing the findings of this report. The Consumer Council's aim is always to work in partnership with stakeholders to produce the best possible outcomes for consumers.

# 8. Appendices

**Appendix 1 - July 2007 – July 2017 average UK house price by UK nation[76]**




[76] https://www.statista.com/statistics/751694/average-house-price-in-the-uk-by-country/

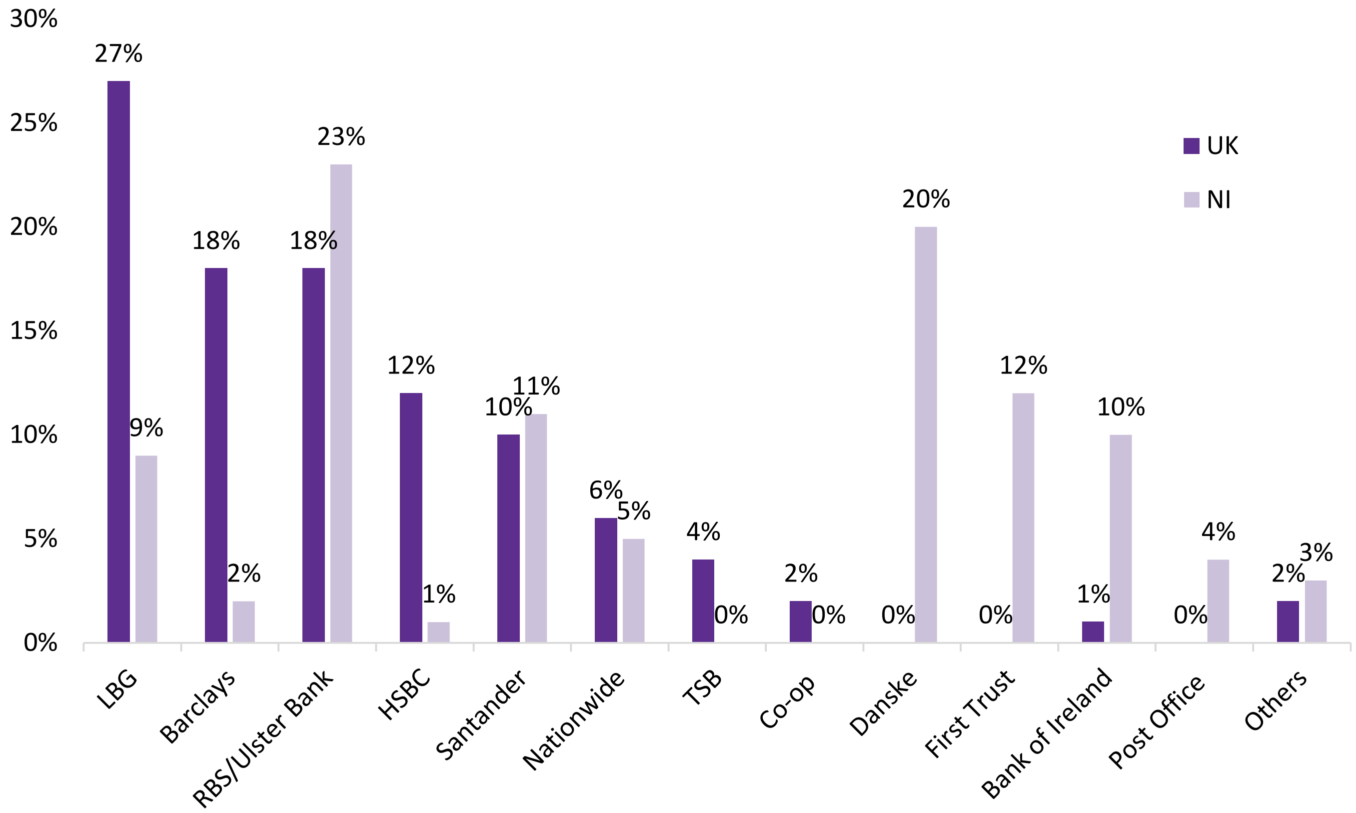
**Appendix 2 – Q3 2007– Q4 2016 first time buyer regional affordability,[77]**

| Region | Mortgage Payments as % of Disposable Earnings | | | |
|---|---|---|---|---|
| | 2007 Q3 | 2015 Q4 | 2016 Q4 | Long-term average (1983-2013) |
| North | 43.8 | 23.6 | 22.8 | 29.1 |
| Yorkshire and the Humber | 40.1 | 23.3 | 22.8 | 28.3 |
| North West | 40.3 | 23.4 | 23.9 | 29.3 |
| East Midlands | 44.1 | 26.2 | 23.2 | 32.7 |
| West Midlands | 47.8 | 27.8 | 28.4 | 35.9 |
| East Anglia | 44.0 | 29.1 | 28.1 | 35.1 |
| South West | 55.2 | 34.1 | 34.3 | 41.6 |
| South East | 55.8 | 40.0 | 41.3 | 46.8 |
| London | 55.8 | 48.3 | 48.6 | 43.5 |
| Wales | 46.6 | 25.0 | 22.3 | 31.7 |
| Scotland | 37.3 | 19.4 | 19.8 | 28.5 |
| Northern Ireland | 63.5 | 19.2 | 20.2 | 28.7 |
| UK | 47.7 | 29.7 | 29.7 | 35.4 |

Sources: Halifax, ONS, Bank of England

[77] http://static.halifax.co.uk/assets/pdf/mortgages/pdf/halifax-mortgage-affordability-2-feb-2017-housing-release.pdf

## Appendix 3 – Market share of NI and UK personal current accounts[78]




[78] https://publications.parliament.uk/pa/cm201314/cmselect/cmniaf/uc650-ix/uc65001.htm; https://www.ukfinance.org.uk/statistics/postcode-lending/

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