The Mortgage outlook

Following the focus on mortgage market issues at last week's Housing Market Intelligence conference, this note summarises the current position for members.

There are two large clouds hanging over the UK mortgage market: funding and regulation.

1. Mortgage Funding

Net mortgage lending (gross lending minus repayments) is running at extremely low levels. In the first eight months of 2010, monthly net lending averaged £0.6bn per month, down from £1.0bn per month in 2009 and around £9bn per month in 2006 and 2007. The CML forecasts net lending of £12bn in 2010, unchanged on last year. This compares with £110bn in 2006 and £108bn in 2007.

The CML has estimated that by the end of 2014 the major lenders will have had to refinance £300bn of outstanding lending temporarily supported by Bank of England and government schemes, with 2011 the peak refinancing year. So far only £50bn of this sum has been refinanced. In other words, the lenders will have to raise a further £250bn simply to stand still. Very recently, there have been some signs that investors' appetite for mortgage-backed securities may be improving. Most notably, RBS has recently successfully undertaken a £4.9bn bond sale. However, the lenders clearly have a very long way to go.

2. Mortgage Regulation

The CML has raised very serious concerns about the potential impact of FSA proposals for tighter mortgage regulation. It is clear the regulations, if implemented, would have a very serious impact on home builders.

In its July consultation, *Mortgage Market Review: Responsible Lending (CP10/16)*, the FSA proposed a number of changes to lenders' assessments of affordability[1].

[1] Looking at the borrowers' expenditure and income, assessing all loans on a capital+interest basis even if interest-only, assessing all on a 25-year basis even if longer, applying a "buffer" to applicants with an impaired credit history, and applying an interest rate stress test.

Both the FSA and CML have assessed the potential impact of the proposals by testing what would have happened if the regulations had been in place between 2005 Q2 and 2009 Q1. However the FSA's analysis was very limited, whereas the CML attempted to assess the cumulative impact of most of the proposed regulations.

In summary, the CML analysis shows that 51% of loans actually granted in the period 2005 Q2-2009 Q1 might not have been granted, some 3.8 million loans, rising to 60% of first-time buyers loans, 80% of borrowers with impaired credit history and 61% of self-employed borrowers. The benefit of the FSA's regulatory proposals would have been to prevent some 151,000 arrears cases and 38,000 possessions.

In short, the FSA's proposals would have a very serious impact on the mortgage and housing markets. In a footnote to the FSA consultation, it concedes its own modelling "did project significant falls in house prices from the reduction in lending".

Our take on the situation is that the FSA has looked at the mortgage market purely as a regulator: because the mortgage market seized up in 2007 and 2008, more regulation must be needed. Its approach seems to involve almost the elimination of any risk, regardless of the wider consequences. However this is to view the issue from the wrong end of the telescope. The question should be: how do we ensure the people of Britain are adequately housed, consistent with a sustainable mortgage market. This is a question for the coalition government, including Treasury and CLG.

HBF will be making a submission to the FSA by the 18th November deadline. We have already, and will continue to raise our concerns with ministers and officials across government. We are also considering joining forces with a range of housing organisations to ensure our concerns receive due consideration by the government and FSA.

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