Household Finance Review – Q4 2020

The fourth quarter review captures the latest data on household activity and finances as the Covid-19 pandemic continues to dominate the landscape. Whilst the UK economy has continued to recover some of the lost output from the Q2 lockdown, many households are still feeling the major financial and social disruptions caused by the pandemic, with incomes remaining under considerable pressure. Throughout the pandemic the financial services industry has worked with government to provide tailored support to households who have found themselves in financial difficulty. Here we look in detail at how the mortgage and unsecured lending markets have fared as Covid-19 continues to impact on the UK.

Eric Leenders, Managing Director, Personal Finance comments:

"Homebuyers looking to take advantage of the stamp duty holiday were behind the housing market's strongest quarter for purchases in 13 years, in the final quarter of 2020. Despite this uptick in activity, annual purchases for the whole year were around a tenth lower than the previous year, due to a complete shutdown of the market in the first lockdown.

"The stamp duty holiday helped to boost activity at the end of 2020, and it is likely many of these purchases have been brought forward in order to take advantage of the savings. The chancellor's announcement in the Budget to extend the Stamp Duty holiday until the end of June before then phasing it out will prevent a cliff edge, reducing the risk of house sales collapsing and will prove beneficial for all parties involved in the housing market.

"There were some signs of increased consumer confidence in unsecured borrowing, with credit card spending growing during the quarter, however this was mixed with the continuing economic uncertainty and further lockdown

HIGHLIGHTS

- **House purchase lending in Q4 grew to the highest quarterly levels since 2007, led by December levels 31% higher than seen a year earlier.**
- **Mortgage lending was lower in 2020 than in 2019 as a result of the decline in lending in Q2, but higher than expected due to the high Q4 activity.**
- **Applications data point to a likely slowing in house purchase activity later in 2021 once the stamp duty holiday has ended.**
- **Remortgages with equity withdrawn have become more popular in Q4 2020, with the average value of money withdrawn increasing, driven by use for deposits for second homes, new buy-to-let (BTL) properties or to assist with deposits for children buying their first properties.**
- **With industry and government support measures in place, Q4 saw only modest rises in arrears and minimal possessions, in line with earlier 2020 trends. While arrears are anticipated to rise in 2021, lenders remain prepared to assist customers and mitigate payments problems.**
- **Whilst credit card lending slowly increased, personal loan borrowing fell and deposits increased further to record highs as households remain cautious against an uncertain economic outlook.**

restrictions which led to a decline in new personal loans.

“The payment deferral schemes, which were in place for most of the last year, have helped millions of customers impacted by covid-19. The plans to gradually ease the lockdown restrictions over the coming months will be a welcome sight for many. However, we know that some customers will still be struggling and the industry is continuing to provide tailored support. Anyone who is facing payment difficulties should contact their lender as soon as possible to get the help they need.”

UK economic context and outlook

The Covid-19 pandemic and the policy and personal responses to it shaped UK economic activity in 2020. The lockdown and social distancing from late March led to an unprecedented fall in UK GDP of 19 per cent in the second quarter of the year. While the adverse effects on the economy were widespread, the service sector, particularly those areas which rely on one-to-one personal social interaction or group activities, was particularly badly affected. The lifting of the national lockdown, but with social distancing largely continuing, resulted in a similarly unprecedented rise in GDP, of 16.1 per cent, in the third quarter. However, the renewed outbreak of the resulting lockdowns in stages during the final quarter of the year, led to a rise in GDP of just 1 per cent.

For the year as a whole, GDP fell by 9.9 per cent, the largest annual fall on record. In the final quarter, GDP was 7.8 per cent below that of the final quarter of 2019, before the pandemic hit. The UK has, of course, not been alone in suffering a massive drop in output, but it saw the largest fall amongst the G7 economies last year. While part of the explanation for the size of the fall is the different way in which the outputs of the education and health sectors are measured in the UK, the UK’s dependence on the service sector, the severity of the effects of the virus, and the prolonged lockdown measures hit the economy particularly hard.

Although the Bank of England reduced Bank Rate from 0.75 per cent to 0.10 per cent and restarted quantitative easing, fiscal policy played a much larger role in supporting the economy. A major part of the fiscal support came in the form of the Coronavirus Job Retention Scheme (CJRS), which greatly mitigated the labour market shocks last year (and, with the extension announced in the Spring 2021 Budget, will continue to do so through to Autumn 2021). As a result, the UK has seen a very different labour market response to the US, where the unemployment rate jumped from 3.5 per cent in February to 14.8 per cent in April as job layoffs escalated. In contrast, in the UK the unemployment rate (which does not include the 3.824 million furloughed employees at the end of December) rose from 4 per cent in February to 5 per cent in November 2020.

As a result of the CJRS, the additional spending on healthcare costs, additional welfare payments, loans and guarantees that were made available to companies, and a Stamp Duty holiday, the UK government has run a fiscal deficit estimated at £364 billion (13.7 per cent of GDP) over the 2020-21 fiscal year. This will raise the public sector debt to GDP ratio above 100 per cent for the first time since 1960-61.

The UK economy started 2021 with a full lockdown in place and economic activity severely curtailed in the service sector in reaction to a second peak in virus infections. At the same time, vaccination rollout began, aiming to reach the most vulnerable groups in the first phase. Following early success in hitting initial vaccination targets, the government has set out a staged roadmap out of lockdown in England, beginning with all schools in England reopening on 8 March. Although each subsequent stage is dependent on a range of conditions being met, the country could potentially see almost all restrictions lifted as early as late June. Similar announcements are expected from the devolved administrations.

On this basis, the National Institute of Economic and Social Research (NIESR) expects that GDP will fall again, by 3.8 per cent, in the first quarter of this year. As with the increase in economic activity last Summer, when restrictions are reduced this year GDP is expected to increase. NIESR projects an increase in GDP of 4.5 per cent in the second quarter and for GDP to continue to increase in the second half of this year and into 2022. Overall, an increase of 3.4 per cent is projected for 2021 and 4.3 per cent for 2022. Even with these increases, it is likely that it will take until the end of 2023 before the level of UK GDP regains its level before the virus struck.

For the labour market, a key uncertainty concerns what happens to the unemployment rate when the furlough scheme ends if restrictions are not yet fully eased. NIESR projects unemployment to rise further, to around 6.5 per cent this year. However with the extension of the furlough scheme announced in the Budget, any significant rise in unemployment is likely to be delayed until the Autumn at least. As in previous recessions and recoveries, the expectation is that it will rise further in 2022, to 7.1 per cent, before gradually falling back in the medium term as economic activity rebuilds.

The signing of the Trade and Co-Operation Agreement with the European Union in December 2020 ought to have ended one source of uncertainty that businesses had faced in the past couple of years. However, it has resulted in short-term uncertainty increasing over some specific items such as documentation of trade and some difficulties in supplying some retail goods to Northern Ireland. Non-tariff barriers and rules of origin will make trade with the EU more difficult than when the UK was in the Single Market. These issues will take businesses time to work through and are occurring at a time when they are coping with the pandemic and the associated restrictions on travel.

Short-term disruptions are likely to continue as businesses become accustomed to the new trade procedures. Key for economic activity in the near-term will be the growth of exports and imports. With consumer spending likely to rise faster than GDP, in part reflecting a gradual unwinding of the sharp rise in the saving ratio seen last year, it is likely that imports will increase at a faster pace than exports.

The continued issues surrounding the virus, including the prospects for removing restrictions, the progress of vaccinations, and the development of new variants of the virus, mean that the outlook for businesses and households remains uncertain. In the labour market, the implications for different age groups, skill levels and geographies of rising unemployment will be critically important. In addition, it is difficult to be definite about how consumers will behave once lockdowns (of varying severity and geographical coverage) end, even with a large proportion of the population vaccinated. Voluntary social distancing, reduced willingness to travel on public transport, increased online purchasing and the high level of working from home have characterised the past year. Some (or all) of these could continue for many people which could lead to protracted difficulties for the 'High Street' retail sector in particular.

After an estimated fall of 11.6 per cent in consumer spending last year, NIESR projects a rebound this year of around 2.6 per cent, with about 6.5 per cent growth in 2022. CPI inflation is expected to rise from just below 1 per cent last year to 1.9 per cent in 2022, although there is significant potential for inflation to over- or undershoot this.

In such an economic environment, Bank Rate is expected to remain at its all-time low of 0.10 per cent through this year and beyond. Stability of policy interest rates will offer a stable background for households and companies to plan their activities. But uncertainty over prospects for incomes and revenues, respectively, remain.

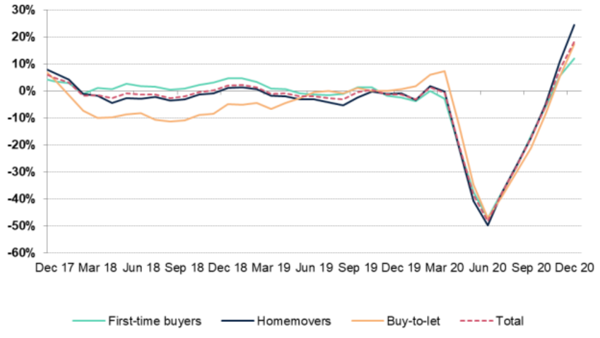
New house purchase activity grew significantly in Q4 2020 as the rush to beat the stamp duty holiday deadline continued

As we observed in our previous Review, the mortgage market in the third quarter of 2020 began to see a recovery from the significant drop in lending in Q2, with growth in purchase activity on the quarter but lower than seen a year earlier. With the stamp duty holiday announced on 8 July 2020, applications in Q3 began to rise as borrowers looked to complete purchases ahead of a potential bottleneck of activity towards the end of March 2021 when the tax break was due to end. With the stamp duty holiday now extended in the government's Spring Budget, this gives borrowers more time to complete deals already in progress and receive the benefits of the stamp duty holiday.

Purchase activity was significantly lower than a year previously in both July and August, but had returned to 2019 levels in September as July applications began to filter through into completion numbers. House purchase completions continued to grow through Q4, reaching an increase of 30 per cent year-on-year in December. Overall, Q4 2020 had the highest volume of house purchase since Q4 2007.

As ***Chart 1*** shows, the V-shaped path of recovery for house purchase saw activity exceed that seen in recent years as borrowers looked to take advantage of the stamp duty holiday.

Chart 1: Number of mortgages for house purchase, 3-month moving average, year-on-year change



Source: UK Finance

Although the year-on-year change in Q4 completions matches that of applications in the previous quarter this recovery is stronger than expected, given the potential for local and national lockdowns put in place through Q4 to disrupt activity. In fact, these proved to have had less impact on completions than anticipated, as lenders put significant resource in to completing purchases as demand increased.

Of particular note in this respect is the buy-to-let market, where Q4 2020 saw the highest purchase activity since Q1 2016 (when landlords looked to complete sales ahead of the introduction of a stamp duty surcharge on second homes). There is some anecdotal evidence that BTL house purchase may remain robust even beyond the stamp duty deadline, with landlords expecting a return to "normal" as the vaccine programme rolls out.

While there is evidence that rental arrears have increased and tenant demand has declined, underwriting standards required by the Prudential Regulation Authority (PRA) has ensured that lending to landlords is affordable, not only at the point of lending but also in the event of adverse economic shocks. This should help ensure that, if rental markets soften as the government support for Covid-19 income support schemes is withdrawn, landlords remain able to maintain their mortgage payments.

The growth in house purchase volumes in Q4 has not been sufficient to recover the lost activity from Q2, where purchase activity dropped by around 50 per cent due to the first set of national lockdowns. Purchase activity was down by around 25 per cent in the first three quarters of 2020, a deficit which had reduced to only 12 per cent by the end of the year (Table 1).

Caution should be taken in directly comparing 2020 to previous years, due to the unique challenges faced throughout the country and the adaptation of the market as the year developed. However, a look at how 2020 compared to a "normal" year does help to demonstrate the impact the coronavirus epidemic had on the mortgage market, and how government and lender support has helped customers.

Table 1: 2020 key mortgage figures

2020 Key Mortgage Figures

	2019	2020	Annual change
Number of house purchase loans:			
First-time buyers	351,000	303,000	-13.7%
Homemovers	344,000	309,000	-10.2%
Buy-to-let landlords	72,300	64,500	-10.8%
Total	767,300	676,500	-11.8%
Number of mortgage refinances			
Residential - external remortgage	446,400	351,800	-21.2%
Residential - internal Product Transfers	1,203,200	1,171,400	-2.6%
Buy-to-let - external remortgage	182,900	158,400	-13.4%
House Prices (UK average, Q4)	215,925	229,819	6.4%
Gross mortgage lending (£ million)	267,932	243,086	-9.3%
Mortgages in arrear (end of year)	75,280	83,260	10.6%
Mortgage possessions	8,000	2,660	-66.8%

Source: UK Finance, Nationwide BS, Bank of England

While there was a decline in house purchase activity in 2020, the market proved resilient despite the significant challenges it has faced. The stamp duty holiday and lender commitment to continue serving borrowers throughout the pandemic has meant that the market ended the year in a stronger position than perhaps anticipated last spring, when the market was put on pause.

It's also important to remember that lenders continue to balance serving customers who need to borrow with their duty to lend responsibly. This is a particularly relevant factor when we look at the total volume of homemovers in 2020, which surpassed the volume of first-time buyers for the first time since 2017.

Homemover volumes overtake First-Time Buyers (FTBs) in 2020 due to affordability and stamp duty

Following the initial set of national lockdowns, lenders withdrew a large number of mortgage products in the face of unprecedented economic and social disruption. These product withdrawals were across all Loan-to-Values (LTVs) but particularly for high LTV mortgage products, which are used disproportionately by first-time buyers and whose deposits are not funded by the sale of a current property.

As a result of the lower availability of higher LTV products, the average deposit for homebuyers in December 2020 was £20,000 higher than a year earlier. We see a similar pattern in the average income of borrowers buying a home, which is over £5,000 greater than a year earlier.

More recently we have seen an increase in product availability. However, this increase is concentrated between 70-90 per cent LTV as lenders continue to exercise caution in a hugely uncertain environment; whilst the lowest deposit mortgages remain less widespread than before the pandemic began.

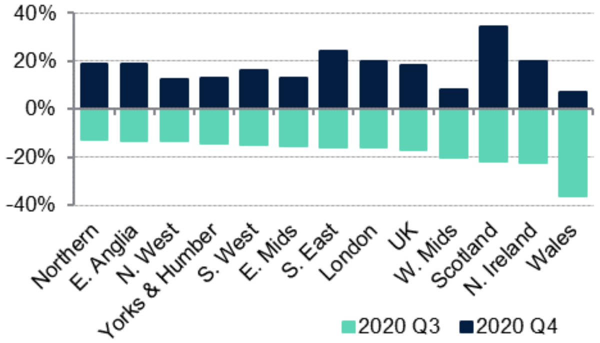
While increased affordability is a large factor in homemover volumes overtaking first-time buyer volumes, the stamp duty holiday also favoured movers more than FTBs. Looking at lending in England, in Q4 2019 approximately 70 per cent of all FTB purchases were exempt of stamp duty. This compares to approximately 5 per cent of homemovers in the same period. In Q4 2020, 92% of FTBs paid no stamp duty, compared to 76% of homemovers, resulting in a greater number of homemovers benefitting.

With the stamp duty holiday benefitting more homebuyers and FTBs impacted by affordability and product availability, we might have expected FTB activity to fall off more sharply than it did last year. A key driver of current activity is the end of the current help-to-buy scheme in March 2021, with borrowers looking to complete purchases ahead of the deadline. While the current help-to-buy scheme will be replaced with a new one this will be less generous, with regional price caps now making some more expensive properties ineligible under the new scheme.

The mortgage guarantee scheme announced in the government's spring Budget will widen access to low deposit mortgages for many and will support lending volumes, in particular to FTBs, to an extent. However at this stage it is too early to fully assess likely impacts.

While stamp duty and help-to-buy has helped to drive purchase levels in Q4 2020, these levels differ when we look the regional picture as in **Chart 2.**

Chart 2: House purchase lending growth, UK countries and regions



Source: UK Finance

The devolved nations saw the biggest year-on-year declines in activity in Q3 2020, in part due to a later opening of the housing markets in these areas. In Scotland and Northern Ireland, there was a significant boost in activity in Q4 as borrowers looked to take advantage of the stamp duty holiday.

There were lower rates of activity growth in Wales and the West Midlands, both of which had seen larger contractions in Q3. It is possible that local lockdowns and the tier system in these areas may have influenced borrowers to hold off their purchases as the Covid-19 situation continued to develop.

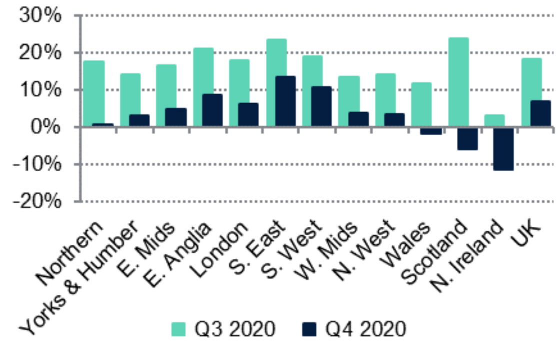
Growth was strong throughout the south of England, which helped to drive purchase activity in the UK as a whole to levels around 20% higher in Q4 2020 than in Q4 2019.

Prospects for further growth in house purchase markets in 2021 are less certain, as the stamp duty holiday ends and the help-to-buy scheme changes. While the stamp duty holiday has helped to boost activity at the end of 2020, it is likely many of these purchases have been brought forward in order to take advantage of the savings. Demand could be commensurately lower for the later part of 2021 as a result.

This is beginning to show in our Q4 mortgage applications data (**Chart 3**), which indicates completions volumes will begin to moderate, albeit that lending is likely to remain elevated through to the end of March as lenders work through the very significant volumes of applications already in the pipeline before the original end date for the stamp duty holiday.

Residential mortgage applications slow in Q4 2020

Chart 3: Number of residential mortgage applications, per cent change year on year



Source: UK Finance

While most regions saw growth in applications in Q4 2020, these began to cool towards the end of the quarter as the original deadline for the stamp duty holiday approached, with many borrowers likely to have brought their purchases forward from later in 2021, anticipating a potential bottleneck in applications in Q1.

The devolved nations saw the lowest applications activity in Q4, while the south of England continued to show strong growth. Again, this is in part likely due to differences in timing of national lockdowns and the differing tier systems.

Completions into Q1 2021 are expected to remain strong as mortgages continue to complete and take advantage of the extended stamp duty holiday.

Refinancing – Internal product transfers grow in popularity

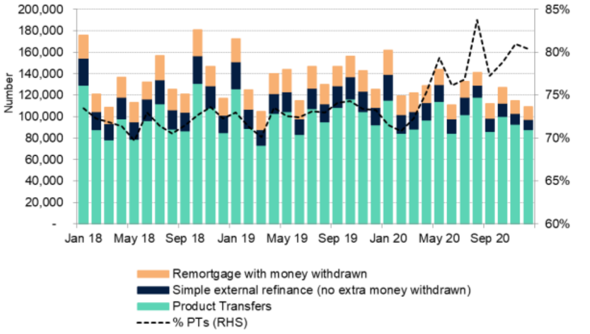
Overall, refinancing remained relatively stable in 2020, compared to the previous year.

Over 1.5 million customers switched their mortgage in 2020, equating to 1 in 6 of all homeowners with a mortgage in the UK. 1.17 million of these were through an internal product transfer, representing £168.3bn of mortgage borrowing refinanced internally.

While this is slightly lower than seen in 2019, the share of internal product transfer refinancing has increased through 2020, as seen in **chart 4**.

We've seen product transfers pick up in popularity over the past two years and have made up around 70 to 75 per cent of refinancing each month since 2018.

Chart 4: Number of residential remortgages and internal product transfers



Source: UK Finance

While overall levels of refinancing were subdued in Q4, due in large part to volume of borrowers coming to the end of their fixed rate deal, we have seen a general increase in the popularity of product transfers.

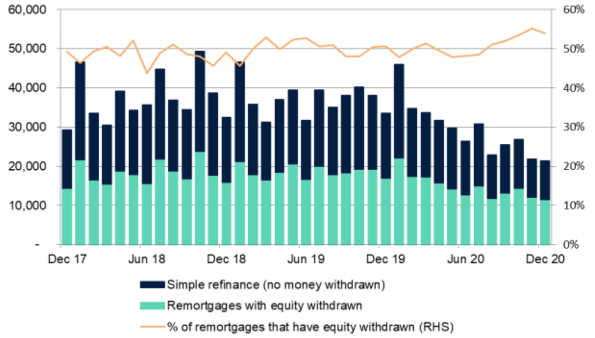
This trend began in May 2020, as the housing market began to reopen. This overlaps with the peak of the volume of mortgage payment deferrals in place (1.8 million). While a payment deferral is in place, customers are not able to take out a new mortgage contract (through an external remortgage) however they are able to internally product transfer due to an industry agreement; this is likely to have driven this trend.

The popularity of product transfers generally has had a further impact on gross lending, in addition to the contraction in house purchase seen in 2020, as product transfers do not feature in gross lending totals.

While external remortgaging has become less popular, there have been recent trends within remortgaging that are worth examining.

As the corollary to the growth in product transfers, simple pound-for-pound external remortgages have fallen away in popularity. At the same time, remortgages with equity withdrawn have grown in over the second half of 2020, as shown in **chart 5**.

Chart 5: Number of residential remortgages by type of remortgage



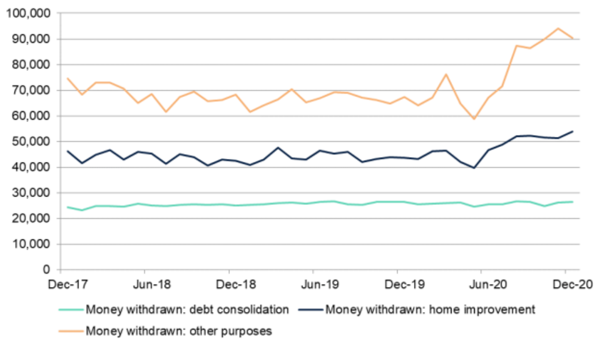
Source: UK Finance

While product transfers will have had a direct impact on the market share of pound-for-pound remortgages, it appears from our data that remortgages with equity withdrawn have also seen a boost in activity in H2 2020 compared to the first half of 2020.

While the increase in equity withdrawal may not appear to be all that significant, it's worth looking at the reasons for which borrowers are withdrawing equity and how much equity they are withdrawing to further understand this trend.

Within our data, lenders report three different reasons for equity withdrawal within a residential remortgage: home improvement, debt consolidation, or 'other'. As we see within ***chart 6,*** borrowers are taking more money out for home improvement or for other reasons, but not for debt consolidation.

Chart 6: Average value of equity withdrawal through residential remortgages (£), by reason for withdrawing equity



Source: UK Finance

On the home improvement side, it's clear that borrowers are using lockdown as an opportunity (or incentive) to expand their homes or to make other improvements. It's also clear from the increase in amounts withdrawn that these are larger than in previously seen, so may be being used to fund more extensive projects.

On money withdrawn for other purposes, we've seen an increase in relatively large amounts of money withdrawn, driving up the average amount of withdrawn money. It is likely that at least some of this is to fund purchases of a second property while the stamp duty holiday is in place. These properties may range from holiday homes to BTL properties.

It is also possible that some borrowers may also be withdrawing equity to provide deposits for children or other family members to buy their first property, which itself could be a phenomenon exacerbated by the expected end of the stamp duty holiday.

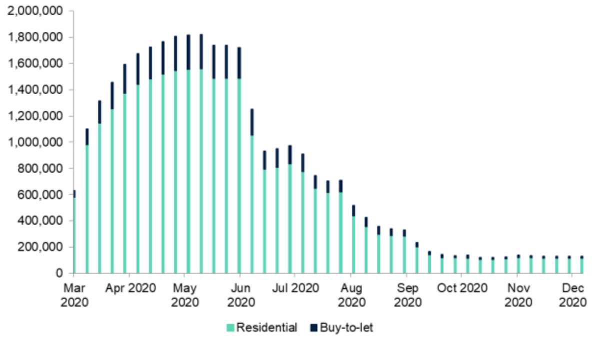
Additionally, we have also seen an increase in equity withdrawal in the BTL sector, albeit on a smaller scale to the residential sector. It appears that landlords are leveraging equity in their existing portfolio to fund new purchases.

Overall, this suggests that borrowers are using equity within their homes to enhance their own (or their family's) housing assets.

Covid-19 related payment deferrals

As **chart 7** shows, the Covid-19 related payment deferral scheme has been running for almost a year. The scheme has slowed in recent months as the majority of customers return to normal payments (**chart 7**).

Chart 7: Number of payment deferrals in place



Source: UK Finance

The number of payment deferrals in place remained high for the four months after the deferral scheme came into effect, after which there was a staggered decline in active deferrals up until October (as covered in our Q3 Household Finance Review).

Payment deferrals numbers declined from 1.8 million at the peak to 135,000 in October. While we might have expected that number to continue to decline, payment deferrals have remained broadly stable up to the end of 2020, with 130,000 still in place at the year end.

This trend is in part due to the extension of the payment deferral scheme, with applications open until the end of March 2021. In fact, though, since mid-October the numbers of new deferrals granted has broadly matched the number exiting the scheme.

In terms of what happens when payment deferrals come to an end, the trends we saw earlier in 2020 have remained broadly consistent in Q4. Around four in five borrowers on a payment deferral returned to full monthly mortgage payments, with the vast majority of the remaining borrowers taking a further deferral. The remaining few borrowers will have repaid their deferral without capitalising or have moved onto business-as-usual (BAU) forbearance.

Lenders are continuing to support borrowers past the end of the payment deferral scheme and have a range of BAU forbearance tools they are able to offer on a case-by-case basis where customers are unable to return to full monthly payments.

Arrears see marginal tick up but remain close to historically low levels

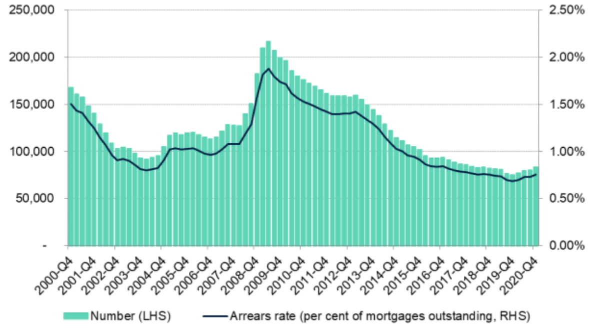
Prior to the onset of COVID-19, arrears had continued to decline to record low levels, driven by record employment figures, the continuing low and stable interest rate environment, and the responsible lending rules in place since 2015, ensuring that all new lending is affordable both at the outset and in the event of adverse income or payment shocks.

The number of mortgages in early arrears increased in Q1 2020, largely due to early payment difficulties prior to payment deferrals being introduced. However, since then, payment deferrals have allowed some borrowers who had found themselves in early arrears to pay these off and prevented additional borrowers from going into arrears. This resulted in a decline in early homeowner arrears in the following two quarters of 2020, larger than the increase seen in Q1.

While the number of these early arrears has increased slightly in Q4 2020, they remain lower than the number of cases before the Covid-19 pandemic began.

As shown in ***chart 8***, the overall number of mortgage arrears has ticked up modestly throughout 2020, but remains close to the low levels seen in the previous few years, as the drop in early mortgage arrears has partly offset the rise in later arrears.

Chart 8: 1st charge homeowner and buy-to-let mortgages in arrears[1]



Source: UK Finance

Notes: 1. Arrears measured as those representing more than 2.5 per cent of outstanding mortgage balance

The volume of borrowers in later arrears did rise in 2020, although this was a gradual increase throughout the year. This led to an overall increase in arrears in Q4 compared to Q3, albeit by modest volumes.

As the number of borrowers struggling to meet their mortgage payments rises, lenders are actively seeking to assist these customers find a manageable path to getting back on track with payments.

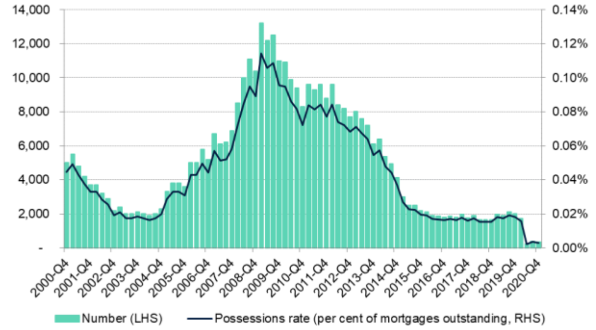
We anticipate that the number of early arrears will increase once the furlough scheme ends in September and the underlying economic impacts of the pandemic start to play out. However, it's important to stress that the industry is prepared for this, with BAU forbearance and other measures to assist borrowers through payment difficulties.

For those worried about not being able to meet their monthly mortgage payments, lenders are keen to help and borrowers are encouraged to contact their lenders early to seek assistance.

Possessions activity remains largely halted

With the industry moratorium on involuntary possessions in effect from March 2020, possessions activity has been almost zero since then (as shown in ***chart 9***). Those possessions that have taken place are cases where the customer requested the possession to go ahead or where the property was vacant.

Chart 9: Number and proportion of 1st charge mortgages taken into possession in period



The industry moratorium remains in place until 1 April 2021. Once the moratorium has been lifted, it is expected that possessions will slowly begin to increase, in line with the backlog of court hearings unwinding.

While we expect possessions to increase, it's important to understand the timelines involved. Taking possession of a property is a lengthy process which is always the last resort for lenders once all other options have been exhausted. Any possessions taken in 2021 will, for the most part, not relate to borrowers who fell into payment difficulties during the pandemic, but will be those borrowers already in possessions proceedings prior to the pandemic.

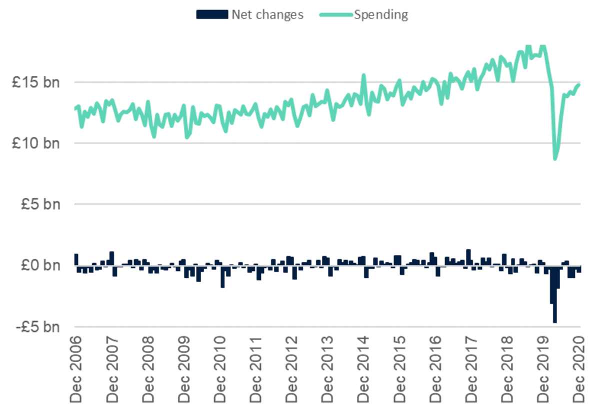
Possession numbers in 2021 will remain relatively low in terms of numbers. Lenders are putting significant resource into helping borrowers to stay out of arrears and avoiding possession proceedings.

Unsecured Borrowing – Credit Cards

Credit card borrowing accounts for around half of all unsecured credit provided by banks and building societies. As reported in our previous Review, spending on credit cards contracted by 25 per cent in Q2 compared to the previous year as lockdown restrictions resulted in a sharp drop in spending in many sectors, including hospitality, entertainment and travel.

As lockdown restrictions eased towards the end of Q2 and more parts of the economy began to open up, new borrowing started to increase again. Borrowing increased slowly throughout Q3. Whilst there were lockdown restrictions again in Q4 borrowing increased by 4 per cent compared to the end of Q3. Despite these new lockdowns, seasonal event such as Black Friday sales as well as Christmas are likely to have contributed to the increased levels of borrowing seen over the quarter. At the end of Q4 borrowing reached £14.8 billion. This compares to a total of £8.7 billion at the peak of lockdown in April (***Chart 10***).

Chart 10: Credit card spending and net changes in balances outstanding



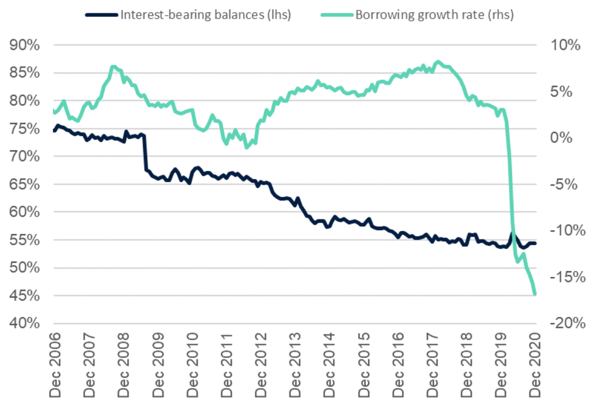
Source: UK Finance

Overall credit card borrowing in Q4 2020 was 19 per cent lower than the same time the previous year. While still at low levels, credit card spending has increased by 22 per cent compared to the end of Q2. This increase is likely be due to the mentioned seasonal events and Christmas, as consumer confidence remains weak with new lockdown restrictions at the back end of the quarter.

Chart 11 illustrates the changes in borrowing on cards – with the initial drop in April mirroring the fall in spending, and also the proportion of interest-bearing credit cards. Over the past decade, the proportion of card balances bearing interest has reduced to 54.4 per cent (down from 66.1 per cent in December 2011) as more credit card customers pay off balances in full when they receive their monthly statements.

At the start of Q2 there was a small increase in the percentage of credit cards bearing interest however, this metric has now fallen and sits at 54.4 per cent as at the end of Q4. Since the start of the pandemic the borrowing growth rate has continued to fall and now sits at negative 17 per cent. This decline indicates that consumer repayments are continuing to outstrip new lending, with many customers opting, because they had significantly reduced outgoings, to pay down debt in the current environment.

Chart 11: Annual growth in card borrowing and proportion of balances bearing interest



Source: UK Finance

As highlighted in the previous review the end-date for the credit card Payment Deferral (PD) scheme was extended to end March 2021, with a long stop date of 31 July. Since the start of the scheme, over 1.18 million credit card PDs have been granted. Similar to the trend seen in mortgage PDs, the number currently in place has fallen since the summer.

Unsecured borrowing – Overdrafts

Borrowing through personal current account overdrafts with banks and building societies had fluctuated around a peak level of around £10 billion between late 2005 and 2009. Since then, the level of overdraft borrowing gradually decreased to just over £6 billion by the end of 2015 and remained at similar levels until early this year (***Chart 12***).

However, in Q2 2020 overdraft borrowing fell sharply to £5.2 billion, and is now slightly below this level at £5.0 billion at the end of Q4 2020. The initial fall in overdraft borrowing in Q2 can be attributed to some customers flexing their household budgets in the face of an uncertain Covid-19-dominated backdrop, to repay borrowing in conjunction with the lower spending we have observed.

Chart 12: Overdraft borrowing

Source: UK Finance

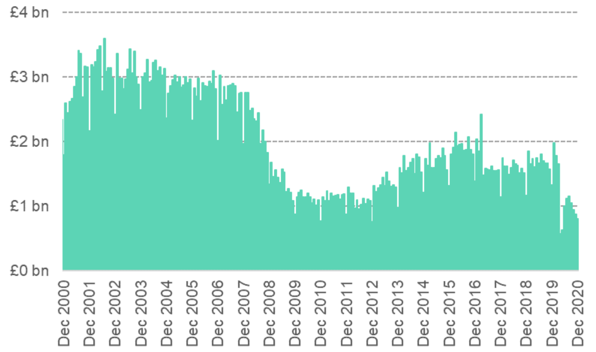
Due to lockdown some customers will have had lower expenses, including reduced travel costs, as well as less opportunity to spend on non-essential retail or social events. Some may have opted to use these additional savings to pay off any outstanding debts. As expenses have declined, customers may also have looked to put these savings into easy access accounts, evidenced by sharp increases in deposits in Q4. Whilst other forms of borrowing such as credit cards increased in Q4 compared to the previous quarter, overdrafts have remained relatively stable. This suggests that overdraft borrowing is often seen as a final option when compared to that on credit cards and loans.

It should also be noted that, in addition to credit card payment deferrals, many organisations have provided customers with personal current account fee-free, interest-free overdraft buffers up to £500. Just over 27 million personal current account holders have had this borrowing relief applied to their account.

Unsecured borrowing – Personal Loans

After rebounding in Q3 after a steep fall the previous quarter, the total amount of new personal loans fell in Q4 and was 21 per cent less than that in Q3 (***Chart 13)***. The initial Q2 decline was largely driven by the adverse economic environment, with lower levels of consumer confidence and fear of rising unemployment seeing consumers cautious in taking on additional debt. After a recovery in Q3 the increasing lockdown restrictions in Q4 have seen consumers once again remain cautious on taking on additional debt as the effects of the pandemic continue to play out.

Chart 13: Amounts of new personal loans from banks



Source: UK Finance

As with credit card borrowing, new applications and extensions to current Covid-19 payment deferrals for personal loans run until the end of March 2021 with a long stop date for deferrals of 31 July 2021. Since the start of the scheme, 828,000 personal loan PDs have been granted but, again, the number in place has dropped away significantly since peaking in the summer.

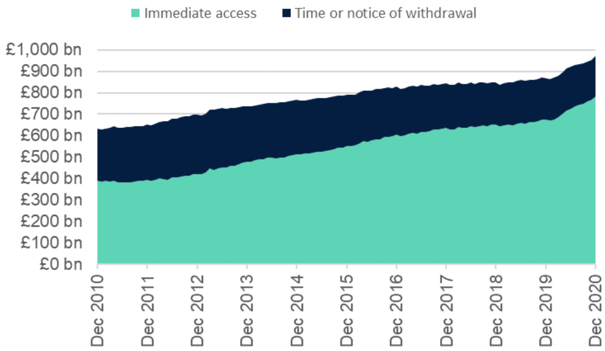
While this is likely to translate into an increase in amounts outstanding in early 2021, it will take some time to see how the various payment deferrals on mortgages and unsecured lending interact at the individual customer level. It will also be important to understand how customers have chosen to use the flexibility of these support measures to manage their personal finances through the current crisis.

Deposits

Recent years' data have signalled a build-up of savings by households. However, these savings have largely been held in easy access accounts, with the low interest-rate environment (both current and expected future rates) dampening demand for term products as there is less incentive to put money into these accounts when easy access accounts have similar rates.

Chart 14 shows that over the fourth quarter of this year deposits continued to grow. During the pandemic many households have had their regular outgoings substantially lower because of COVID-related restrictions, but have also looked with increased uncertainty at their future finances and employment prospects and postponed or forgone spending, resulting in a steep rise in savings of 10.3 per cent compared to the end of Q1.

Chart 14: Personal deposit account balances



Source: UK Finance

In Q3 as the economy showed signs of improvement the rise in deposits slowed, however this has increased again as lockdowns were once again put in place. This suggests that households remain cautious, which tallies with recent consumer confidence indices that indicate increased plans to save, and with economists' expectations of a growth in the savings rate during the pandemic.

Whilst total deposits grew by 3.8 per cent over the quarter this was due the growth of immediate-access accounts, with time deposits actually falling by 1.3 per cent. Households have chosen to prioritise the ease of access of savings in these accounts in uncertain times over the rates of returns held in fixed accounts such as ISAs, with the total amount of savings held in in ISAs declining by £2.4 billion over the quarter.

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