# Household Finance Review

In this review we look at activity in UK households' finances in the third quarter of 2019.

There are 28 million residential properties in the UK and more than a million sales a year. Mortgage lending supports nine million residential property owner-occupiers and a further 200,000 buy-to-let landlords in the private rented sector.  Unsecured credit products allow households to manage their spending, with over 60 million personal credit cards (more than two per household), while personal current accounts are used for holding deposits due to their immediate access and overdraft facilities.

**Eric Leenders, Managing Director, Personal Finance comments:**

*"Reflecting on the year so far, there have been steady levels of activity in the home purchase lending market, which is likely to be linked to affordability, rather than weakening consumer confidence in the economy, despite uncertainty surrounding Brexit.  Against this backdrop, mortgage refinancing activity has increased, driven by the availability of attractive longer term fixed rates.*

*Even though borrowers were pessimistic about the wider economy, the majority feel optimistic about their household finances. Healthy funding markets and lower interest rates have meant borrowers have been able to access longer repayment periods and lower rates.  Unsecured borrowing using personal loans, overdrafts and credit cards has declined as the build-up of savings increases, indicating customers are taking careful borrowing decisions."*

## 2019 Q3 HIGHLIGHTS

- **New residential mortgage lending decreased fractionally in the year to September, compared with the same period last year.**
- **Whilst the buy-to-let market remains in retreat, increased demand from incorporated landlords offers signs of a potential return to growth.**
- **Remortgaging remains strong, but the growth in longer-term fixed rates is starting to bear down on demand for new deals.**
- **With these trends set to continue we expect further modest declines in both the home purchase and remortgage markets next year, and for the buy-to-let market to level off.**
- **Credit card borrowing growth continues to decline and is at its lowest point since 2013.**

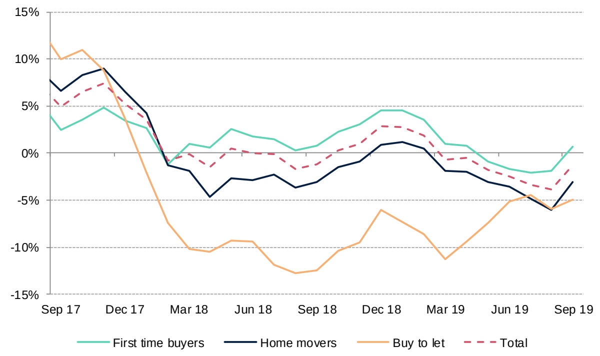
The path of new lending for home purchases so far this year has been one of gentle moderation overall. Within this, the residential sector saw growth in the early months of the year, both for first-time buyers and homemovers, which more than offset the continuing decline in buy-to-let purchase activity.

More recently however, we have seen activity in the residential sector ease off, becoming negative first for homemovers and subsequently for first-time buyers through Q2 and into Q3 (***chart 1***).

At the same time, the buy-to-let (BTL) sector has seen broadly a mirror image of that pattern: whilst activity continues to shrink, the rate of contraction has been moderating since the early months of the year.

Overall, home purchase mortgage numbers for the first nine months of 2019 are around 1.5 per cent down on the same period last year.

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



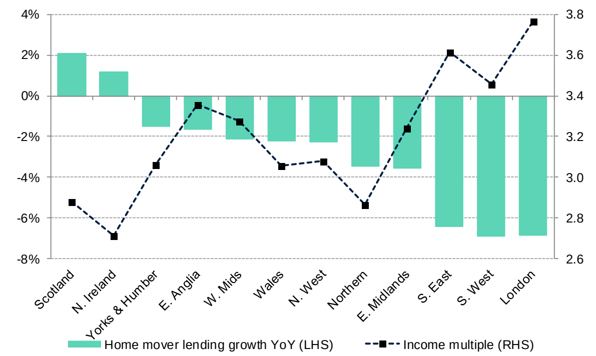

*Source: UK Finance*

Whilst this moderation coincides with weakening consumer confidence in the economy, we have seen little evidence that this lack of confidence extends to the housing market, with reported intentions to buy relatively strong in recent months.

Instead, the easing in activity this year looks to be more strongly correlated with affordability pressures. Under normal market conditions, these hit first-time buyer activity most significantly, not least because they do not have the cushion of housing equity that homemovers have built up, particularly after a period of strong price growth.

What we are seeing this year is a stronger negative correlation between affordability and activity rates amongst homemovers ***(chart 2)***.

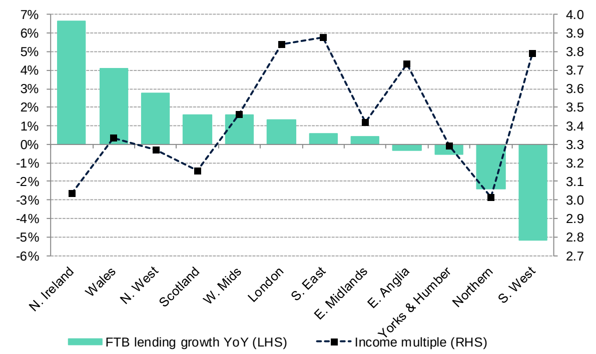
***Chart 2: Homemover lending growth v average loan to income multiple – Q3 2019***




*Source: UK Finance*

First-time buyer activity is also strongest in those regions of the country with more forgiving affordability metrics. However, numbers are also showing positive, albeit weak, growth, in and around London and the South East - where affordability is most stretched ***(chart 3).***

***Chart 3: First-time buyer lending growth v average loan to income multiple – Q3 2019***




*Source: UK Finance*

In the first-time buyer market the Help-to-Buy schemes in England, Scotland and Wales have greatly eased the deposit constraint, which under normal conditions is a significant obstacle for many.

Further significant help comes in the form of the "Bank of Mum and Dad", with the most recent estimates from the Survey of English Housing suggesting almost four in every ten recent first-time buyers get help from their family in funding their deposit.

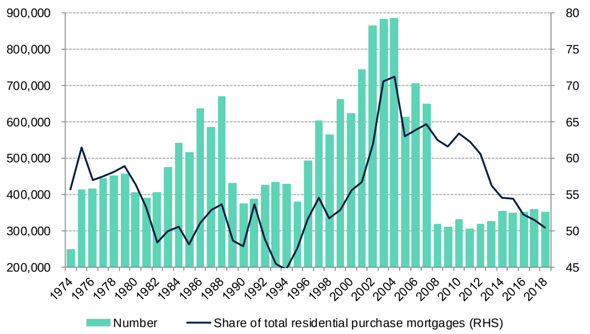
Homemovers, however, have had less recourse to either of these sources, and so have fewer tools to mitigate the growing affordability squeeze.

A second brake on homemover activity comes not from affordability, but a reduced pool of potential buyers. Help-to-buy, whilst a welcome boost for those accessing the scheme, is available for new-build property only, and its continuing significance for first-time buyer numbers bears down on the demand for second-hand property. Meanwhile, the continuing contraction in the BTL market also decreases demand for existing property, particularly in the lower price brackets.

These factors mean that would-be movers, most significantly those looking to make their first move (the "second steppers") are constrained both by an affordability squeeze and a smaller number of potential buyers for their property.

Accordingly, barring the brief period of growth early this year, homemover numbers have been in negative annual growth territory since the beginning of 2018, and remain around half the levels seen in the mid-2000s. Homemovers now take up 50 per cent of total residential purchase mortgages, the lowest share since the early 1990s (***chart 4***).

***Chart 4: Homemovers annual number of loans and share of total residential purchase mortgages***



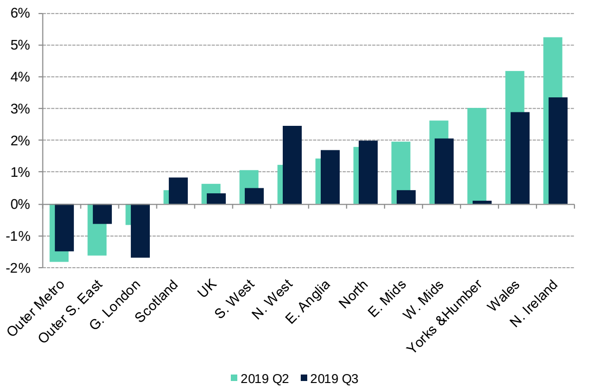

*Source: UK Finance*

Whether this comparative strength in first-time buyers and decline in movers is a healthy long-term dynamic remains to be seen. In the current environment it does seem likely to remain the norm for the time being, and the change in Help-to-Buy to become a first-time buyer-only scheme from 2023 may in fact exacerbate the trend.

## Price growth moderating in most regions

As we have already seen, home purchase activity is constrained across most regions, and particularly so for homemovers. This is also shown in a moderation in house price growth. Although London and the South East remain the only areas in negative territory, Q3 also showed an easing in growth across the majority of English regions, as well as Wales and Northern Ireland (***chart 5***).

***Chart 5: House price annual growth***



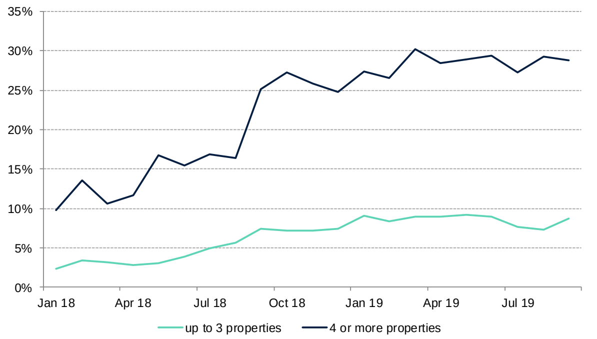

*Source: Nationwide Building Society*

## Signs of stability for the buy-to-let market?

Much has been written about the profound impacts of tax and regulatory change in the BTL sector over the past few years. Indeed, the effects have likely not yet been fully felt; in particular, the phased removal of tax relief for landlords' mortgage interest payments does not complete until tax year 2020/2021, and this will place further pressure on landlords' bottom lines next year.

As we can see from chart 1 BTL activity, whilst still in negative territory, has shown signs of stabilising. There are emerging signs that, although new business from individual landlords remains constrained, there is increased demand from landlords who are set up as businesses (which are unaffected by the tax changes which relate to personal income tax only). This looks to be particularly the case for landlords with larger portfolios. (***chart 6)***.

***Chart 6: Share of buy-to-let purchase activity to incorporated investors[1]***




*Source: UK Finance*

*Notes: 1 data series covers lending to all borrower sectors excluding individuals and unincorporated businesses*

At this stage, the increased borrowing by incorporated BTL businesses has yet to fully compensate for the drop off in activity amongst unincorporated landlords. However, should these trends continue, we may see BTL activity begin to grow again, driven now by an expanding Limited Company BTL segment.

## Refinancing, fixed rates and the future

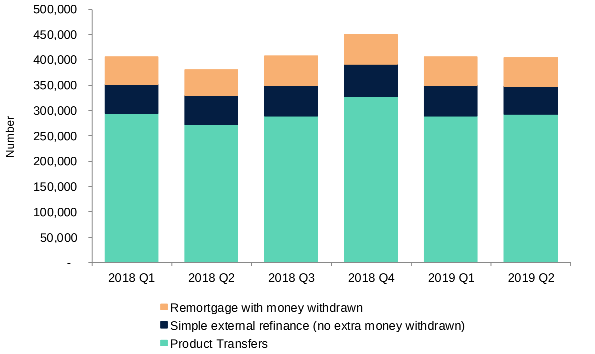
With the continuing pressure on purchase markets, the refinancing markets take on greater importance. This is the case both for borrowers looking to take advantage of continuing attractive fixed rate deals in the face of an increasingly uncertain economic environment, and for lenders seeking to retain both market share and existing customers.

As the Financial Conduct Authority found in its Market Study, customer engagement is high in the UK mortgage market. This is evidenced by our figures for both internal refinancing ("Product Transfers") and the external remortgage market. Combining these segments some 1.6 million residential mortgage borrowers took out a new deal in 2018, which equates to nearly one in five of all mortgages outstanding.

Within this, almost three quarters were internal Product Transfers, which offer borrowers a simpler process if they just require a better rate with no additional money withdrawn. Part of the strength, particularly in the Product Transfer market, followed the voluntary industry agreement to contact all existing borrowers sitting on lenders' Standard Variable Rates who could benefit from a new deal and offer them these deal rates.

Even without this, refinancing was strong in 2018 and remained so this year. In 2019 to date there have been a little over 1.2 million refinancing transactions, 3 per cent more than in the same period last year (***chart 7)***.

***Chart 7: Number of residential remortgages and internal product transfers***

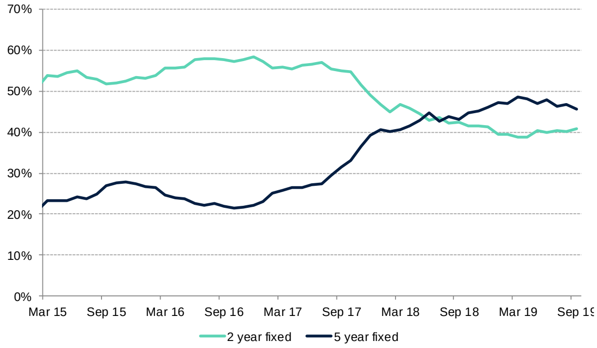



*Source: UK Finance*

Going forward, the refinancing markets may struggle to maintain quite the same momentum, and this is due to the changing nature of borrower preferences. Specifically, more borrowers are now opting for mortgage deals fixed for longer periods - in particular five year fixes which, thanks to healthy funding markets and market expectations of interest rates staying lower for longer, are competitively priced.

This has allowed borrowers to fix their mortgage payments at lower rates for longer periods, which brings a welcome insurance in uncertain times. So far in 2019 almost half of new mortgages were fixed for five years or longer, compared to around a quarter in 2016 when the clear borrower preference was for two year fixes (***chart 8***).

***Chart 8: Share of two and five year fixed rates, new residential lending***




*Source: UK Finance*

A secondary effect is that the shift to longer term fixes pushes out the maturity schedule, so that fewer borrowers each year reach the end of their deal rate (at which point they are free to move to a new one without incurring early repayment charges).

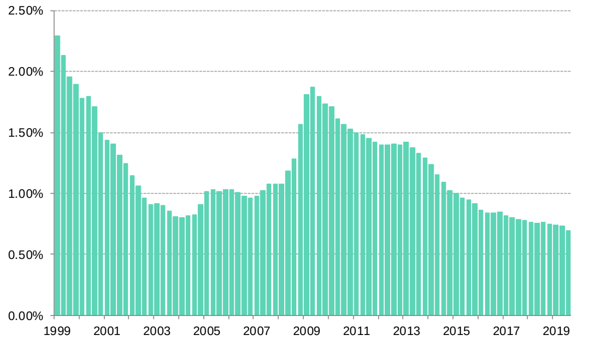
As chart 8 shows, the drop off in two-year fixes in favour of five year deals began in earnest in late 2017. This means that we will start to see a larger drop off in maturing fixed rates from the end of this year, which is likely to bear down on the demand for remortgages.

## Arrears continue to fall

Consumer confidence indicators continue to suggest a majority of borrowers feel optimistic about their own household finances, even though they are pessimistic about the wider economy. There are two key drivers to this – the continuing low interest rate environment and the ongoing strong performance of the labour market.

With unemployment at historic lows and the economy at virtually full employment, an overwhelming majority of mortgage borrowers are able to meet their mortgage payments at these low interest rates. As a result, we are continuing to see arrears levels fall. As at the end of Q3 2019, there were 76,100 mortgages in arrears, an historic low (***chart 9***).

***Chart 9: Proportion of all 1st charge owner-occupier and buy-to-let mortgages in arrears (defined as arrears of more than 2.5 per cent of mortgage balances)***




*Source: UK Finance*

With numbers this low there is limited room for continued improvement; there will always be some borrowers who, through unemployment or other external factors, cannot meet their mortgage payments even at the current low interest rates. However, with new lending since 2015 underpinned by strict stress-tested affordability as required by the FCA, residential mortgage borrowers have a cushion against foreseeable financial difficulty. Barring an unexpected material increase in either unemployment and/or interest rates, we are unlikely to see a significant reversal of the current trend.

The decline in arrears this year has not been echoed in figures for mortgage possessions. In the year to September, some 4,000 homeowner mortgaged properties, and a further 2,000 BTL properties, were taken into possession. Whilst these numbers remain incredibly low by historic standards, this nonetheless represents a 15 per cent rise on the same period of 2018.

Rather than indicating any change in lenders' treatment of borrowers in arrears, the recent rise in possessions is explained by an unwinding of a temporary cessation in possession activity in previous periods, whilst lenders adjusted their procedures to ensure compliance with new FCA guidance on treatment of customers in arrears.

With this unwinding process largely complete, there is reason to expect possession trends will realign with those we continue to see in mortgage arrears.

## The outlook for 2020

Looking ahead to next year, as we have set out, we expect a continued moderation in residential purchase markets, driven by underlying affordability pressures increasingly rippling out from the South East across the country.

Purchase activity in the BTL sector is expected to stabilise, as increased demand from incorporated landlords offsets any additional decline in volumes to individuals.

The remortgage markets, as we also described above, will be constrained by a reduced flow of "free-to-move" fixed rate mortgages coming to the end of their deal period.

We also explore these themes in detail, as well as others that are shaping today's mortgage market in our joint research report with Hometrack, published earlier this month.

We also expect a marginal increase in arrears and possessions numbers, commensurate with a similarly small rise in unemployment from its current record low levels. As we set out above, with only marginal increases in both unemployment and interest rates over the forecast horizon, arrears and possessions numbers will also remain close to their current historic lows.

Our full forecasts for 2020 and 2021 are set out in Annex 1 of this document.

As an essentially domestic market, our mortgage forecasts are underpinned by the factors we have described above.

The December general election, and the Government's future decisions on the UK's departure from the EU, have the potential to change the macroeconomic outlook, including for the labour market and interest rates.

Our broad assumption in making this forecast was that the UK would leave the EU under terms similar to the Withdrawal Agreement negotiated by the Johnson Government and put to parliament.

This scenario is assumed to be neutral with respect to these macroeconomic factors as they impact the housing and mortgage markets.

## Unsecured Borrowing – Credit Cards

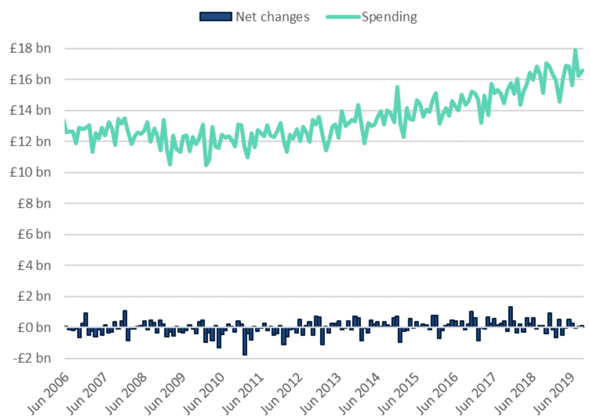
Borrowing on credit cards accounts for around a half of all unsecured credit provided by banks and building societies. With a long period of benign interest rates and strong market competition, annual growth in card borrowing started to expand in 2013 and peaked in early 2018 at over eight per cent, since when it has been declining and now stands at under half that annual rate at 3.4 per cent (***chart 10***). Over the past decade, the proportion of card balances bearing interest has fallen from three-quarters to a half ***(chart 10***).

***Chart 10: Annual growth in card borrowing and proportion of balances bearing interest***


*Source: UK Finance*

The amount of monthly spending on credit cards has been trending upwards since 2013 and is a third higher than it was then. The removal of the credit card surcharge from January 2018, along with cardholders benefiting from spending rewards, loyalty points or protection of goods and services has contributed to increased usage. Spending is, for the most part, largely offset by bill payments from cardholders managing their spending effectively. This is also evident thorough increased numbers of cardholders using Direct Debits to pay more than the minimum amount. This has resulted in the annual net change in amounts outstanding being significantly lower in the year to Q3 2019 than in the previous two-year periods (***chart 11***).

***Chart 11: Credit card spending and net changes in balances outstanding***

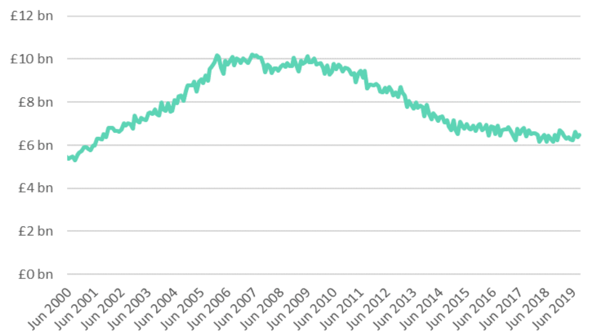



*Source: UK Finance*

## Unsecured borrowing – Overdrafts

Borrowing through personal current account overdrafts with banks and building societies was at a steady peak of around £10 billion between late 2005 and 2009. Since then the level of overdraft borrowing has gradually fallen to just over £6 billion at end Q3 2019 (***chart 12***).

***Chart 12: Overdraft borrowing***

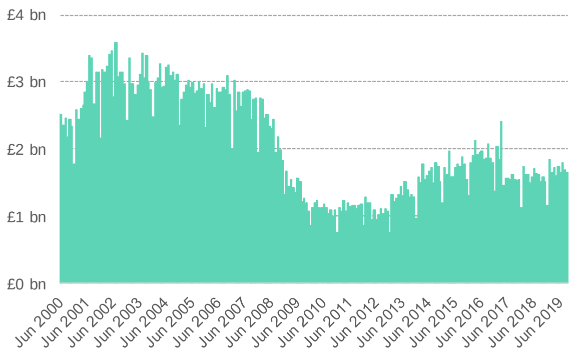



*Source: UK Finance*

## Unsecured borrowing – Personal Loans

Demand for personal loans from banks and building societies has not recovered to levels seen before the financial crisis and, during 2013 – 2019, has been subdued, in part because of consumers choosing the popular alternative of personal car finance plans provided by dealerships rather than applying for traditional bank loans (***chart 13***). For homeowners, another attractive borrowing option might be to increase their mortgage borrowing, taking advantage of the historically low rates that remain available in that market.

***Chart 13: Amounts of new personal loans from banks***

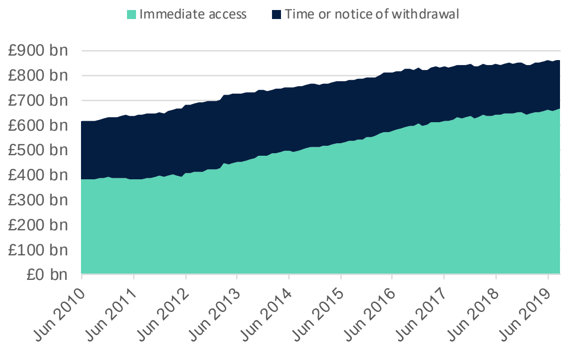



*Source: UK Finance*

## Deposits

The lower use of overdrafts and reduced demand for personal loans has been associated with a build-up in savings. In recent years, deposit growth has been driven by reduced consumption and a return to real earnings growth. Households are typically holding their money in immediate-access accounts, rather than in notice or savings accounts (***chart 14***) and, while low investment returns play a part, quick access to disposable income in uncertain economic times is the driving force for individuals when managing household budgets.

***Chart 14: Personal deposit account balances***




*Source: UK Finance*

## *Disclaimer*

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# Annex 1: UK Finance Mortgage Market Forecasts, December 2019

| Property transactions | | 2014 | 2015 | 2016 | 2017 | 2018 | *2019* | *2020* | *2021* | Source table |
|---|---|---|---|---|---|---|---|---|---|---|
| Number of residential property transactions (000s) | Total | 1,219 | 1,230 | 1,235 | 1,220 | 1,191 | *1,181* | *1,168* | *1,163* | PT1 |
| **Gross mortgage lending** | | **2014** | **2015** | **2016** | **2017** | **2018** | ***2019*** | ***2020*** | ***2021*** | **Source table** |
| Total (£ billion) | Total | 204 | 221 | 247 | 261 | 269 | *264* | *254* | *257* | MM8 |
| Of which: for house purchase (£ billion) | Homeowners | 109 | 113 | 124 | 132 | 135 | *137* | *134* | *133* | RL3 |
| | Buy-to-let | 12 | 16 | 15 | 12 | 11 | *10* | *10* | *11* | MM17 |
| Of which: for remortgaging (£ billion) | Homeowners | 44 | 52 | 64 | 72 | 82 | *79* | *76* | *79* | RL4 |
| | Buy-to-let | 15 | 22 | 25 | 26 | 29 | *29* | *26* | *26* | MM17 |
| **Product Transfers** | | **2014** | **2015** | **2016** | **2017** | **2018** | ***2019*** | ***2020*** | ***2021*** | **Source table** |
| Value (£ billion) | Homowners | N/A | N/A | N/A | N/A | 158 | *164* | *141* | *147* | RS1 |
| **Net mortgage lending** | | **2014** | **2015** | **2016** | **2017** | **2018** | ***2019*** | ***2020*** | ***2021*** | **Source table** |
| Net lending (£ billion) | Total | 24 | 35 | 41 | 46 | 44 | *46* | *38* | *37* | MM13 |
| **Mortgage arrears and possessions** | | **2014** | **2015** | **2016** | **2017** | **2018** | ***2019*** | ***2020*** | ***2021*** | **Source table** |
| Arrears | Total 1st charge mortgages in arrears representing over 2.5% of the outstanding balance | 114,400 | 101,600 | 93,600 | 86,000 | 82,400 | *74,900* | *77,900* | *81,000* | AP2 |
| Possessions | Total 1st charge mortgaged properties taken into possession | 20,900 | 10,200 | 7,700 | 7,400 | 6,900 | *8,000* | *8,100* | *8,300* | AP4 |

Source data tables are available to UK Finance members or data associates from www.ukfinance.org.uk/industry-data/industry-data-tables/.
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