Household Finance Review – Q1 2021

This review explores trends in household financial activity through a quarter that began with a national lockdown in response to a spike in Covid-19 infections and ended with optimism from the early successes of the vaccination programme. Although many households have seen their finances come under pressure, the financial services industry has worked with government to support those who have found themselves in difficulty. Here we look in detail at how the mortgage and unsecured lending markets have fared as the country starts to emerge, cautiously, from the seismic upheavals of the past year.

Eric Leenders, Managing Director, Personal Finance comments:

"Since the housing market emerged from its shutdown last spring, we have seen a remarkable recovery in demand, which continued through Q1 2021.

"Existing homeowners have taken advantage of the stamp duty concessions, with changing working and living patterns encouraging more to use their existing equity, either to move further afield or to fund further housing purchases for themselves or family.

"Towards the end of the quarter, cautious optimism was also evident through modest increases in card spending and in unsecured borrowing.

"The continuing support network for household incomes and credit payments has prevented significant increases in arrears. As the country emerges from lockdown and these schemes come to a close most will be able to resume normal payments. However, for those unable to do this, the industry stands ready to help with tailored support to best suit individual customers' needs."

HIGHLIGHTS

- **House purchase lending surged in Q1 following the rush of applications submitted ahead of the original Stamp Duty Land Tax (SDLT) holiday deadline**
- **Homemover activity was particularly strong, with anecdotal evidence of many homeowners using their substantial existing equity stakes to move to larger properties away from city centres in response to changing working and living patterns**
- **Refinancing remains dominated by internal Product Transfers. However, we continue to see a trend of significant and growing amounts of equity withdrawn with other remortgages, in large part to fund additional property purchases**
- **Payment deferrals and government support for jobs and incomes kept arrears increases in check in Q1 2021, while the ban on court actions meant there were no enforced possessions for the fourth consecutive quarter**
- **From Q2, as support schemes wind down and possessions resume, we are likely to see arrears rise above their current level and, after a lag, possessions rise as well**
- **Credit card borrowing fell due to additional national lockdowns and post-Christmas seasonality but showed signs of recovery towards the end of the quarter**

UK economic context and outlook

The economic backdrop to this quarter's Household Finance Review (HFR) continues to be shaped by the impact of, and policy response to, the Covid-19 pandemic. A continuation of the national lockdown, particularly affecting hospitality, leisure, non-essential retail and other contact-intensive services weighed on growth at the start of this year. In the first three months of 2021 UK GDP contracted by 1.5 per cent, leaving the economy 8.7 per cent smaller compared with pre-pandemic levels.

Unsurprisingly, household consumption was a particular drag on the economy at the start of the year, falling nearly four per cent in the first quarter, following a 1.7 per cent decline in the final three months of 2020. Household consumption is now 12.8 per cent down on pre-pandemic levels. Trends in the first quarter were driven by weakness in retail sales, a further slump in spending in hospitality and hotels and declining spend on transport – all predictable consequences of the lockdowns imposed.

Nevertheless, the overall decline in output was less than expected as parts of the manufacturing, construction and health and social care sectors contributed positively to GDP and some businesses adjusted to public health restrictions with new business models. Moreover, there were some positive indicators emerging at the end of the quarter, with the economy expanding by 2.1 per cent month-on-month in March, supported by production sectors and the reopening of education.

As noted in last quarter's Household Finance Review (HFR), despite the UK economy experiencing the biggest contraction in modern times last year the labour market has shown more resilience than expected. The government's furlough scheme (or Job Retention Scheme), extended again in the March budget, has played a significant part in underpinning this resilience. At the start of 2021, labour market indicators were a little firmer than expected. The most recent data from the Office for National Statistics (ONS) pointed to an increase in the employment rate and a decrease in both the unemployment and inactivity rates in the three months to March. That said, total hours worked declined, again in response to continued restrictions on activity. Further positive signs can be found in the reduction in numbers away from work, both those receiving pay and unpaid, while those on partial pay remained stable.

In response to the planned reopening of parts of the economy, there has been a notable uptick in job vacancies, reaching the highest level since the start of the pandemic although still below levels seen previously. The return of *hiring intentions* is consistent with improving business activity indications, such as the purchasing managers' indices across all major segments of the economy.

With the economy reopening in line with the government's roadmap, together with the rapid pace of vaccine roll-out in the UK, forecasters have made successive upgrades to the growth outlook in recent months. Looking in more detail at the potential path for growth in the remainder of this year set out in the UK Economic Outlook from the National Institute of Economic and Social Research (NIESR), GDP is expected to expand by 5.7 per cent, a stronger outlook than the 3.4 per cent growth forecast in February.

In addition to monetary and fiscal policy remaining supportive of growth, a key contributor to this brighter outlook is a recovery in household spending, expected to rise by nearly six per cent this year. The government's furlough scheme has provided some insulation for household incomes through the pandemic and there has also been a rapid increase in the savings rate over the past year, a result of reduced opportunities for spending. With a fall in savings, together with expectations of some wage growth this year and assuming spending patterns return to pre-pandemic norms, growth should see some support from household spending during 2021.

The latest retail sales data for April from the ONS indicate that consumers are getting back to normal with the reopening of non-essential retail. Particularly strong growth in sales volumes were seen in clothing and other specialist stores.

It is equally important to note that the pandemic has impacted unequally across households in different income brackets. While many households have experienced limited financial detriment from the pandemic, others have been less fortunate, and are likely to experience further stress in the coming quarters.

The NIESR continues to expect further increases in unemployment over the course of this year. The unemployment rate is forecast to peak at 6.5 per cent at the start of next year, which assumes around 450,000 of those on furlough will not be taken back on when it ends later this year. Caution around optimism related to short-term labour market trends is warranted as businesses may wait until lockdowns end and the various job retention schemes close before being able to better assess future plans.

While the improving growth outlook is to be welcomed, the UK is making up lost ground rather than paving the way for an economic boom. Risks to the outlook are also balanced. There are potential upsides if the unlocking of the economy remains on track and accumulated savings are spent more quickly than forecast. Continued concerns about new Covid-19 variants means that the next stage of unlocking is not yet certain which could lead to a more cautious approach to spending and investment by households and businesses.

Housing market resurgence: reasons to be cheerful?

After a year of seismic disruptions – to social interactions, the physical and economic health of the nation and to the operation of the housing market – some signs of optimism in the first quarter pave the way for a brighter outlook in 2021.

Throughout the pandemic the continuing government and industry support programmes have minimised negative impacts on existing mortgage borrowers, while the Stamp Duty Land Tax (SDLT) holiday helped boost demand amongst those with the means to transact.

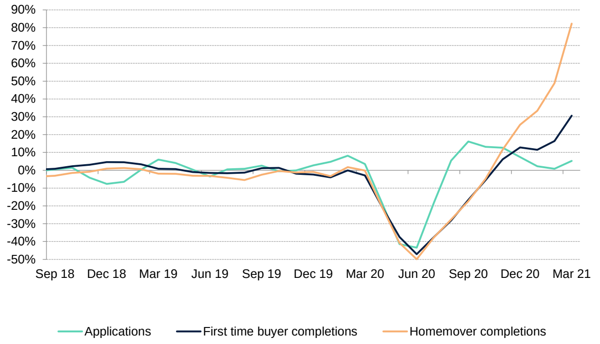
The collapse in house purchase volumes in Q2 last year was inevitable, given the closure of the housing market for most of that quarter. However, the strength of the subsequent bounce back has surpassed expectations in terms of both its magnitude and longevity.

With the stamp duty holiday originally set to end on 31 March 2021, the industry had anticipated a surge of activity in the months leading up to this date. The strength of demand since the reopening of UK housing markets last summer, further fuelled by the temporary tax break, presented a potential test of the industry's resources.

Recognising this, many advisers, anticipating a potential bottleneck towards the end date, counselled prospective borrowers to submit mortgage applications early to maximise the chances of completion before that date.

These factors led to an unprecedented flood of applications beginning at the start of Q3 2020 and accelerating rapidly. This then fed through to commensurate growth in loan completions, which had returned to annual growth by the end of Q3 2020, and then accelerated through to the end of Q1 2021 (***Chart 1).***

Chart 1: Mortgage applications and completions, three-month moving average, year-on-year change



Source: UK Finance

Recognising the potential for a logjam towards the end of Q1 2021 mortgage lenders responded and, since late 2020, put significant additional resource into processing these increased volumes by the original 31 March 2021 end date.

The flow of applications moderated through Q4 2020, in part due to the increased social restrictions as the Covid-19 infection rate rose again. However, in Q1 2021 – despite the second national lockdown – consumer confidence was buoyed by the early successes of the vaccination programme and the prospective (albeit gradual) easing of social restrictions.

This confidence, together with the announced extension of the end date for the stamp duty holiday, led to a second wave of demand, shown in applications numbers in late Q1. This second wave came even as completions – those from applications submitted early so as to beat the original deadline – were already showing high double-digit annual percentage growth.

Homemovers emerge from the shadows

As ***Chart 1*** shows clearly, the strength in the housing market since last summer has been seen for all buyers, but most significantly amongst homemovers.

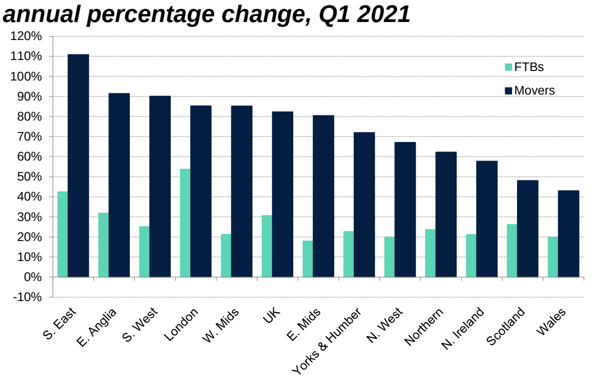
This revival in homemover activity follows a long period of muted transaction volumes dating back to the late 2000s. Since then, first time buyer (FTB) numbers – boosted by a range of successive government initiatives designed to stimulate demand – had recovered to 2007 purchase levels by 2018. However, in that downturn homemover numbers fell to around half the level seen in the years immediately preceding and have remained around those levels ever since.

The help for new buyers over the past decade or so is both welcome and important, with FTBs providing important liquidity at the entry level of the market, thus helping chains to form. However, the absence of such targeted support for existing owners, together with some of the support for FTBs focused specifically in the new build sector (and therefore not part of a larger housing chain), has seen a shift in market dynamics such that fewer existing owners have been able to move up the housing ladder than previously.

A peculiar consequence of the pandemic has been this rebalancing of the market, in a way that market intervention has not previously achieved. One of the reasons is that the marginal benefit of the current stamp duty holiday accrues mostly to homemovers and landlords, because the majority of FTBs across most of the UK were already exempt, through the FTB-specific holiday which had been in place since 2017.

However, another, more fundamental, driver of the strength in homemover activity can be seen in the regional picture (***Chart 2***).

Chart 2: Number of new house purchase loans, annual percentage change, Q1 2021

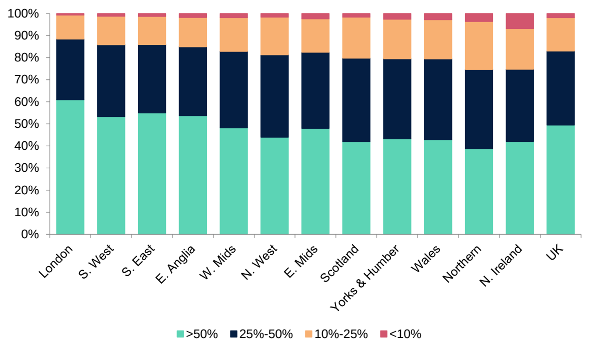


Source: UK Finance

Although each region of the UK saw strong double-digit annual growth in FTB numbers in Q1, homemover growth vastly outpaced this in every region. While exceptionally strong everywhere, the strongest growth rates were in the south east, where volumes rose 110 per cent compared with a year ago, and the other southern regions of England.

To unpick this further, we need to look at the role of existing equity and house prices. ***Chart 3*** shows the amounts of equity held by current mortgage borrowers, based on their current property value and remaining mortgage balance.

Chart 3: Equity stakes of residential mortgage borrowers, December 2020.



Source: UK Finance

Overall, UK borrowers' equity positions (as a proportion of the current property value) are strong. Following around nine years of uninterrupted price growth, half of all mortgaged homeowners have at least 50 per cent equity in their home, and a further third have between 25 and 50 per cent.

There is substantial regional variation; this is particularly important in the current environment and a key contributor to the strength in homemover activity. Equity stakes are strongest in London and the southern regions, where up to 60 per cent of borrowers own at least half of their home's equity outright.

This translates to sizeable amounts of housing wealth: nationally, one in five borrowers have more than £250,000 of equity, approximately the average house price in the UK (according to HM Land Registry data).

In the south east, with both higher proportional equity stakes and property values, this rises to more than half of borrowers. In London, one in five borrowers have more than half a million pounds of free equity in their property, more than enough to buy an average priced property in every other region of the UK.

In normal times, the greater amount of equity in these southern regions is no more or less "useful" than in areas with lower prices, as most people move within their own broad region. However, the pandemic, bringing with it increased homeworking as well as significantly increasing the importance of both outside and inside space, is changing this dynamic.

It has always been the case that many homeowners in London, unable to afford larger property locally to accommodate an expanding household, move to the outer suburbs and the commuter belt where space is more affordable. The difference this time is the magnitude.

As we observed above, homemover numbers had been running at around half of their typical levels in 2005-2007 ever since the Global Financial Crisis (GFC). However, in Q1 2021 activity leaped by 82 per cent compared to Q1 2020, bringing volumes to a level not seen since 2007.

The pattern of transactions – exceptionally strong in London but even stronger in the regions surrounding, including those not previously thought of as commuter belt – suggests a mini-exodus, albeit one which has been accentuated by the original stamp duty holiday end date in March. Increased numbers of homemovers are moving out, not only of their immediate locality but to regions further afield than would have been the case in previous years.

Data from HM Land Registry suggests at least some are cashing in their equity and buying outright, as the latest figures (to December 2020) indicate significant increases in the proportion buying without a mortgage in every region of the UK. Our own data show many more are using their equity plus mortgage borrowing to achieve space, location and other desirable attributes in a new area.

The pandemic has brought with it a need for space during lockdowns. However, the strength of this housing market response, coupled with a steady trickle of newsfeeds as to employers adapting their homeworking policies for the long term (and, more recently, greater flexibility around part-time rail season tickets), points to at least the potential for a more fundamental shift in the patterns of homebuying.

While London and other cities will always remain important commercial centres, the ability of many to work from home in perpetuity, whether for all or part of each working week, has allowed more UK households to re-evaluate not only what they most need from their home but where that home is located.

It remains to be seen whether this is a temporary shift which will revert, once the pandemic and its aftershocks have subsided, to the pre-existing preference for London and other large cities.

However, should it prove more permanent and pervasive, this has the potential to lead to other economic phenomena including some rebalancing of property prices more evenly across the country, as well as revitalisation of local high streets and wider economies.

Buy-to-let activity matches homemovers

At the same time as this unprecedented surge in homemover numbers, the buy-to-let (BTL) sector has also seen significant growth, with mortgages for BTL house purchase increasing by 59 per cent in Q1 2021, compared to a year previously.

The stamp duty holiday has been a significant demand stimulus in the BTL sector, where new purchases attract a three per cent second-home stamp duty surcharge on top of the prevailing rate for residential homebuyers.

However, the surge in purchase activity followed a broadly similar regional pattern as for homemovers, with London and the other southern regions showing the strongest growth. This is likely to reflect landlords responding to increased demand from households seeking to move for the same reasons as detailed above for homemovers, but who at this stage are looking to rent properties rather than buy.

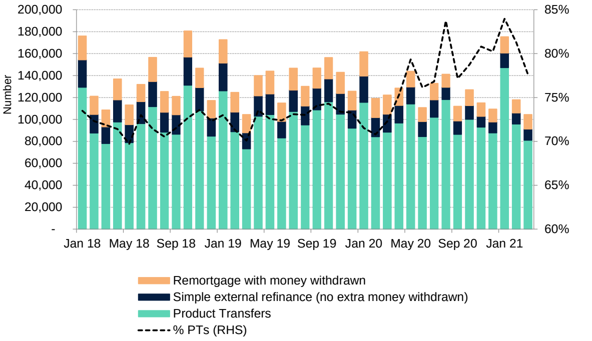
Looking ahead, demand from both homemovers and BTL landlords is likely to start to moderate as the stamp duty holiday comes to a staged conclusion through to the end of Q3. Beyond this point, the outlook is less clear. To the extent that the societal changes to where people want to live persist, the regional demand patterns we have seen recently may continue.

Internal product transfers saw a New Year lockdown boom

Refinancing saw a large spike in January 2021. This is fairly typical behaviour; remortgaging sees a boost as each year begins and consumers put their finances in order after the festive season.

This January, the spike came almost entirely from Product Transfers (PTs). Nearly 150,000 PTs were completed in January 2021, 27 per cent up on a year previously and the highest monthly number on record (***Chart 4***).

Chart 4: Number of residential remortgages and internal product transfers



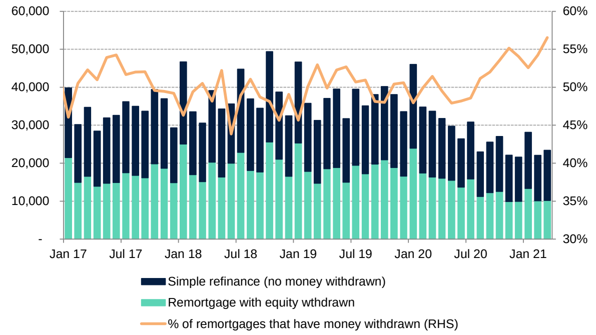
Source: UK Finance

This is likely due to the second lockdown that was in place; for the first time this January's normal refinancing surge took place under conditions that hindered access to mortgage advisers and further heightened the attraction of PTs, which can be transacted without advice and via remote channels, including online.

In fact, the increase in January was seen almost entirely for execution-only, online transactions. Although there remains a thriving external remortgage market, the ease with which PTs can be carried out when unable to physically visit an adviser, as well as the industry agreement to allow customers on a payment deferral to take out a PT, has helped 1.1 million customers manage the cost of their housing finance through the pandemic.

In addition to the January surge in simple refinancing, Q1 saw a continuation of another remortgaging trend which we observed in our Q4 2020 Review. Although the strength in refinancing numbers has been concentrated in the internal PT sector, the external remortgage market remains robust. Within this market, the proportion of remortgages where extra money is taken out has seen a steady increase through the past 12 months, reaching 57 per cent of all internal remortgages by March (***Chart 5***).

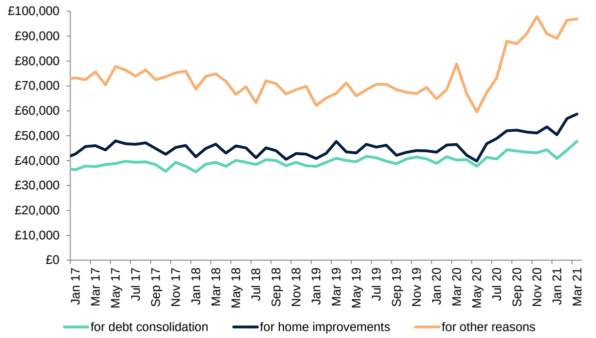
Chart 5: Number of residential remortgages by type of remortgage



Source: UK Finance

This trend has been fairly steady, if unspectacular compared with the surge in purchase activity. What is more noteworthy is the amounts withdrawn, which have increased very significantly since mid-2020 (***Chart 6***).

Chart 6: Average value of equity withdrawal through residential remortgages by reason for withdrawing equity



Source: UK Finance

These increases have been more pronounced amongst those remortgages where the money is withdrawn for home improvements and, even more so where the equity is for "other reasons". Both contextual and anecdotal evidence suggest one of the most common "other" reasons for withdrawing such a sizeable sum is to fund, either in part or in full, further property purchases. This could be for BTL, second homes or gifted deposits for family members.

Although the shift to greater amounts withdrawn is seen in all regions, the absolute amounts withdrawn – again linked to regional property values – are important. The amounts withdrawn in London rose more rapidly than in other geographies to £189,000 by March 2021 ***on average***. This is enough to buy an average-priced property in any UK region outside the south of England, and a sizeable majority equity share in any of the southern English regions.

As with the current boom in homemover activity, a mixture of the stamp duty holiday and changing patterns of living and working are likely to have fuelled these trends, whether this is for owner-occupied, holiday or rental property.

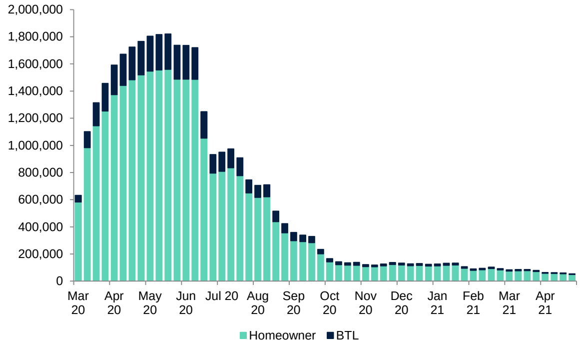
There will ultimately be a limit on the extent to which those more property-rich homeowners are able to leverage their existing property assets to expand further afield. We can see further ways in which existing borrowers appear to be accessing accumulated equity to help respond to the challenges and opportunities presented by the ongoing situation.

Covid-19 related payment deferrals

On 31 March 2021, just over a year after it began, the Covid-19 payment deferral (PD) scheme closed to new applications. Given the country was still in lockdown throughout the first quarter, and well over four million employees were still on furlough, we might have expected some increase in applications as the scheme drew to a close.

In fact, there was no material uptick in applications, and the small numbers received were more than offset by the volumes coming to an end. As such, we saw the total numbers of PDs in force continue to decline, albeit gradually, to just under 80,000 by the end of March (***Chart 7***).

Chart 7: Number of payment deferrals in place



Source: UK Finance

With the scheme now closed, we will see the numbers in force continue to ebb away through to the end of July 2021, when any final three-month deferrals put in place in March will conclude.

For customers exiting the scheme, we have seen a fairly consistent figure of eight in ten borrowers capitalising the deferred payments and returning to full payment.

In most of the remaining cases the borrower took a further payment deferral where this was available. Only a small number moved immediately on to tailored support or more established forbearance measures, the nature of which is designed to best suit the customer's particular circumstances.

With the PD scheme now closed, both for extensions and new applications, the final path of customers exiting their arrangement depends hugely on the evolution of the labour market as the country emerges from lockdown – a process now well underway – and the furlough scheme is wound down.

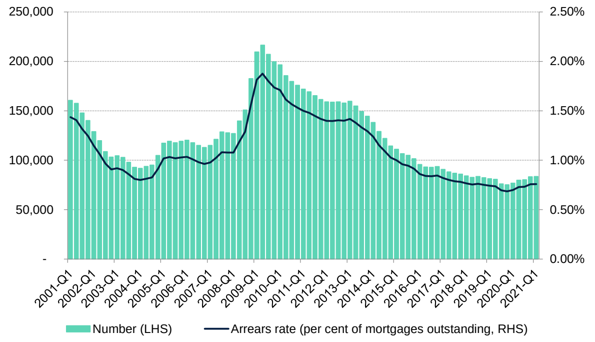
We can reasonably expect most furloughed employees to be able to resume work, and at the same time any self-employed, who have been unable to do business in lockdown conditions, to resume trading. However, to the extent that some proportion will inevitably not be so fortunate, we are likely to see some increased volumes of customers in need of tailored support through Q2 2021 and beyond.

While this tailored support will provide invaluable help for customers it is important to note that, in contrast to the PD scheme, arrears are reported while the customer is in receipt of BAU forbearance. While the PD scheme did not add to arrears numbers, customers in a reduced payment arrangement will have arrears accruing, albeit at a slower rate than if making no payment at all.

Support schemes keep arrears at bay, despite second lockdown

Since the country first went into lockdown in March 2020 we have seen continual, but modest, increases in overall arrears numbers. In Q1 2021 this continued, with an increase of just 360 arrears cases to 83,600 (***Chart 8***)

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

Within the total, however, there are some important trends. Early arrears – those where the shortfall represents 2.5 and five per cent of the balance outstanding – have fallen as some customers have been able use the time on a PD to pay down modest arrears and return the account to performing status.

However, at the other end of the spectrum those in the higher arrears bands, in particular cases representing more than ten per cent of the balance, increased by a slightly higher number than the reductions at the lighter end.

These heavier arrears take some time to accrue, particularly with the historically low interest rates that have been in place since the last market downturn in the late 2000s. These customers' payment issues may potentially have been exacerbated by the pandemic, but this was not the initial cause of their financial difficulty.

While these longer-term arrears cases are an ongoing concern, they are likely to be receiving BAU forbearance or be under active arrears management.

However, over the past few years very few customers have newly experienced arrears, either personally or potentially even second-hand from the experience of family or friends.

This is due in part to the more stringent underwriting requirements which have been part of Financial Conduct Authority (FCA) responsible lending rules since 2014. These rules ensure that all homeowner mortgages are affordable and have a buffer to ensure that they remain affordable in the event of a degree of adverse payment or income shock.

The evidence is that these rules appear to be working as intended and that this has continued through the pandemic. However, as the furlough and PD schemes end, some customers whose incomes are disrupted for a longer period will find themselves in this position, many for the first time.

For this reason, it is more important than ever that borrowers who find themselves in financial difficulty speak to their lender, as the industry stands ready to help its customers.

Many BTL landlords able to absorb increases in rental arrears

Although we have seen only modest rises in total arrears numbers, the picture is different when we look across sectors: homeowner arrears have increased only modestly, with those increases concentrated in the heavier bands. In the BTL sector, however, increases have been seen across all bands, and by a greater degree.

In total there were 5,970 BTL mortgages in arrears in Q1 2021, eight per cent up on Q4 2020. Although this is a larger percentage increase than in the homeowner sector, it is important to bear in mind that the increase is from a very low base and, therefore, small in absolute size; in total, the cumulative increase in BTL arrears cases since March 2020 translates to only 1,550 landlord mortgages.

As with most trends over the past year, the disproportionate growth in BTL arrears appears linked to the pandemic. The labour market impacts, while widespread, have disproportionately impacted on young people and lower-paid workers, two groups who are significantly more likely to be renters than homeowners.

Growth in BTL arrears looks to be concentrated amongst landlords with small portfolios – one or two properties. Those with larger portfolios have been able to defray the lost income from tenants who have suffered through the pandemic and are unable to make their rental payments.

Although there are considerably more small-portfolio landlords (by number) than larger-scale ones, the majority of the BTL mortgage stock is held by the larger ones (a mathematical result of those larger portfolio sizes). Therefore, if this pattern continues, increases in BTL arrears are likely to be limited. However, the industry will continue to monitor the sector for any changes and respond to developments as accordingly.

Looking ahead, despite well-founded optimism arising from the success of the vaccination programme and easing of lockdown, we do nonetheless expect arrears cases to rise, both in the homeowner and residential sectors, once income and payment support schemes come to a close.

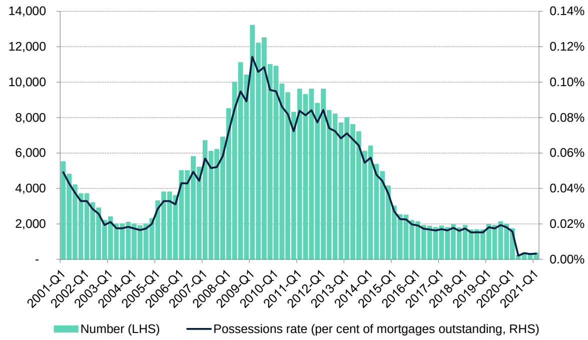
As before, the industry stands ready to help with tailored support that best suits each customer's circumstances and help them get back on track. Our message remains clear: customers experiencing financial difficulty should talk to their lender at an early stage – they are ready to help.

Possessions activity remained minimal in Q1, but gradual increases now expected

The moratorium on involuntary possessions ended in November. However, a temporary ban on bailiff enforcements, supported by a voluntary industry agreement not to enforce possessions during mid-winter, meant that both Q4 2020 and Q1 2021 saw only minimal possession activity.

There were just 360 possessions in Q1, again confined to only those which have taken place at the customer's request or of vacant properties (***Chart 9***).

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



Source: UK Finance

As of 31 May 2021, the ban on bailiff enforcement of evictions also ended in England (and is expected to end on 30 June 2021 in Wales), and normal possession activity can resume. Given the length of the moratorium there is now a material backlog of possession cases that, under normal conditions, would have taken place.

These cases, which we estimate to number around 5,000-6,000, need to take place in the customers' best interests, to prevent further accumulation of debt and any erosion of remaining equity. However, we do not anticipate a flood of activity in Q2 2021, rather a more measured increase each month as both courts and lenders deal with this backlog in a manageable and sensitive fashion.

Looking beyond Q1, the ban on rental evictions ended on 31 May. However, the courts will deal with these cases in a similarly sensitive fashion and the additional protections which apply to residential homeowners also apply to BTL landlords with respect to their tenants.

Because the PD scheme has greatly mitigated increases in arrears, we do not expect to see any material increase in "new" possession activity (that is, cases arising from Covid-19-related payment issues), until the end of this year at the earliest. Lenders will work with customers in arrears and explore all other viable options to get back on track. Possession, as always, remains the last resort once all other options have been explored.

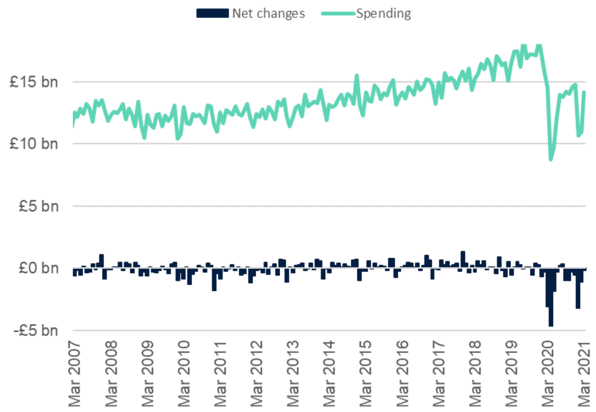
Unsecured Borrowing – Credit Cards

Credit card borrowing accounts for around half of all unsecured credit provided by banks and building societies. As reported in our previous review, lockdown restrictions at the start of the pandemic in Q2 2020 saw spending on credit cards contract by 25 per cent compared with the previous year as spending dropped in sectors such as hospitality, entertainment and travel. This then started to recover during Q3 as lockdowns began to be lifted and more sectors of the economy opened up over the summer, with this recovery slowing during Q4 as parts of the country saw subsequent lockdowns.

At the start of Q1 2021, further national lockdowns as well as lower seasonal spend post the Christmas period saw total spending in the quarter decline by 17 per cent from the previous quarter, and fall by 24 per cent compared with Q1 2020, with decreases concentrated in the same lockdown-sensitive sectors.

Borrowing did increase at the end of the quarter, reaching £14.2 billion. This compares with a total of £10.7 billion at the start of the quarter in January 2021 and £8.7 billion at the peak of the first lockdown in April 2020 (***Chart 10***). This may be a reflection of consumers starting to become more confident of their future economic outlook following the rollout of the vaccine program and the announcement of a timetable for gradual easing of restrictions.

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



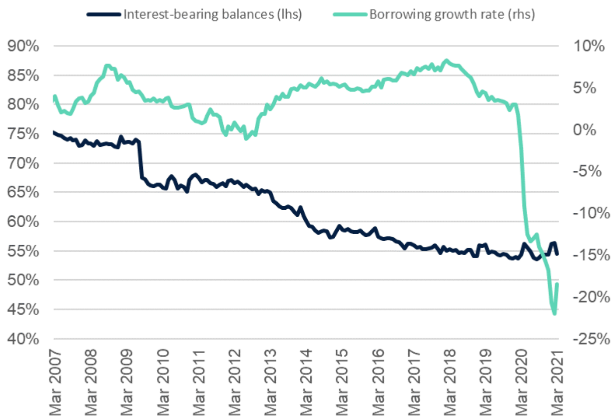
Source: UK Finance

While still at low levels, credit card spending during the lockdown in Q1 2021 is 17 per cent higher when compared to that seen during the first lockdown in Q2 2020. This suggests this lockdown has not had as severe an effect as the initial one in April 2020.

Chart 11 illustrates the changes in borrowing on cards – with the initial drop in April 2020 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 54.6 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 quarter there was a small increase in the percentage of credit cards bearing interest, likely due to the effect of spending over the Christmas period at the end of the previous quarter, however this metric has now fallen and sits at 54.6 per cent as at the end of March. Since the start of the pandemic the borrowing growth rate has continued to fall and now sits at negative 18 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 credit card Payment Deferral (PD) scheme ended on 31 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 last summer.

Unsecured borrowing – Overdrafts

Borrowing through personal current account overdrafts with banks and building societies 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 2020 (***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 Q1 2021. 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

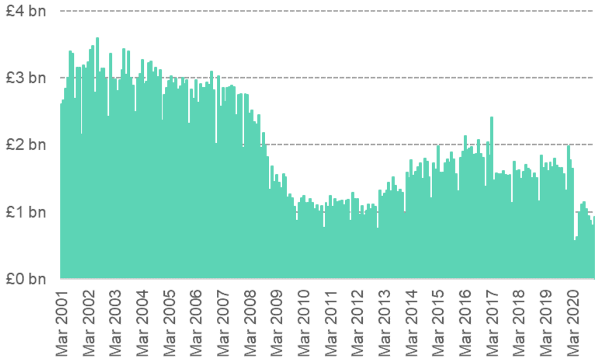
Some customers are likely to have had lower expenses during periods of lockdown, including reduced travel costs, as well as less opportunity to spend on non-essential retail or social events. This may have resulted in some opting to use these additional savings to pay off any outstanding debts. As expenses have declined, customers may also have looked to put these savings into easy access accounts, evidenced by increases in deposits since the start of the pandemic. While other forms of borrowing such as credit cards have slowly increased from their initial drop at the start of the pandemic, overdrafts have remained relatively stable since the initial drop in April 2020. This suggests that overdraft borrowing is often seen as a final option when compared with that on credit cards and loans.

As mentioned in the previous review, in addition to credit card payment deferrals, many organisations provided customers with personal current account fee-free, interest-free overdraft buffers up to £500. Just over 27 million personal current account holders had this borrowing relief applied to their account in 2020.

Unsecured borrowing – Personal Loans

After falling in Q4 2020, the total amount of new personal loans increased by 21 per cent in the first quarter of 2021 (***Chart 13***). This rise was largely due to an increase in loans taken out at the back end of the quarter in March. This is likely due to consumers starting to become slightly more confident about the economic environment as both the vaccine rollout gathered pace, and a timetable for lifting restrictions was put in place.

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 ran 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.

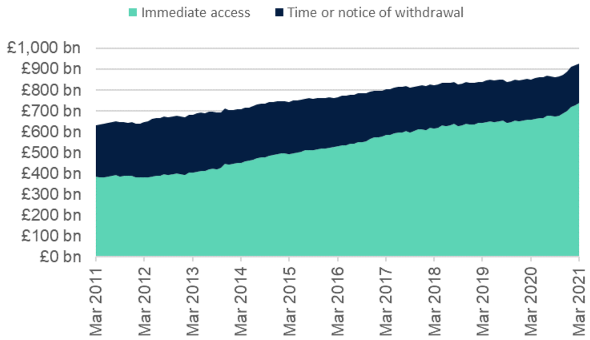
While this is likely to translate into an increase in amounts outstanding in mid-2021, it will take some time to see how the various payment deferrals on mortgages and unsecured lending interact at the individual customer level. It will also be important to understand how customers have chosen to use 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 first quarter of this year deposits continued to grow. During the pandemic many households have had their regular outgoings substantially lower because of Covid-19-related restrictions, but they 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 16.3 per cent compared to the end of Q1 2020.

Chart 14: Personal deposit account balances



Source: UK Finance

In Q4 2020, as the economy showed signs of improvement the rise in deposits slowed, however this accelerated again in Q1 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.

Total deposits grew by six per cent over the quarter, with both access accounts and time deposits increasing by seven per cent and 1.7 per cent respectively. Households have chosen to prioritise the ease of access of savings in access 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 £10 billion between Q1 2020 and Q1 2021.

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