Household Finance Review – Q4 2021

This review explores trends in household spending, saving and borrowing through the final quarter of 2021. Confidence dipped slightly amidst uncertainty around the rapid spread of the Covid-19 Omicron variant but, with the economy remaining largely free from social restrictions, activity levels remained relatively buoyant. Here we look in detail at how the mortgage and unsecured lending markets fared as the second year of the pandemic drew to a close.

Lee Hopley, Director of Economic Insight and Research, said:

"Although household spending and borrowing were more subdued at the end of last year, activity levels continued to return to pre-pandemic norms.

"House purchase numbers fell in the fourth quarter following the end of the stamp duty holiday, although there are signs of continued demand for more space as working from home becomes a part of regular life. Looking ahead, the rising cost of living will likely affect appetite to buy or move home this year.

"It is encouraging that arrears are still trending down, with no early signs yet of any difficulties in repaying unsecured debts. However, while households look to be in a good position regarding payments now, we expect some increase in arrears through the year as the rising cost of living starts to bite.

"Any customers worried about meeting their loan repayments should speak to their lender as soon as possible to discuss the best options for them."

UK economic context and outlook

HIGHLIGHTS

- **Spending and unsecured borrowing took a slight dip amidst uncertainty surrounding the spread of the Omicron variant**
- **House purchase lending dropped sharply in Q4 following the end of the Stamp Duty holiday, but demand looks to be relatively resilient, underpinned by longer-term changes in life and work patterns as we emerge from the worst of the pandemic**
- **The same factors continue to drive an increase in equity withdrawal when remortgaging for reasons of home improvement**
- **The rising cost of living has yet to impact but is likely to bear down on effective demand for mortgages, particularly amongst lower income households.**
- **Mortgage arrears are still trending down and as yet there are no early signs of problems in unsecured borrowing. However, payments are likely to come under greater pressure through 2022 as the cost-of-living squeeze weighs more heavily.**

The UK economy grew by one percent in the fourth quarter of 2021. Services and construction registered positive growth for the quarter, whereas production output fell further below pre-pandemic levels, in large part due to a fall in gas and energy supply. Services activity continued to be buoyed by growth in the health sector, driven by increased GP visits at the start of the quarter and Covid-19 testing and tracing activities in December. UK GDP is estimated to have grown 7.5 per cent in 2021, technically making it the fastest growing economy in the G7. However, it is important to note that this is following a rebound from a particularly weak 2020, during which the UK registered the second largest contraction of the seven economies.

The Omicron variant emerged in the latter half of the fourth quarter, with new cases of Covid-19 exceeding 100,000 a day towards the end of December. However, the resulting rise in staff absences and voluntary social distancing did not have a significant impact on the economy, with GDP falling by only 0.2 per cent in December. This left output in the UK economy at the same level as February 2020, just before the pandemic began.

There are mixed signals coming from recent labour market indicators. Following the end of the Coronavirus Job Retention Scheme (CJRS) in the close of the third quarter, unemployment continued to decline to 4.1 per cent in the three months to November, only 0.1 per cent above pre-pandemic levels. However, employment remains 600,000 below March 2020, largely driven by a decrease in self-employment.

There has also been an uplift in economic inactivity as an increasing number of young people entered education during the pandemic, and more recently a rise in the number of reports of ill health and early retirement being reasons for workers leaving the labour force.

As well as falling unemployment, job vacancies rose to record levels again in the fourth quarter, with every industry registering a rise. This combination signals a tightening labour market for the UK, with the unemployed per vacancy ratio reaching a 50-year low. Surveys suggest employers are facing recruitment difficulties, which has translated into underlying pay growth of around four per cent (as estimated by the Bank of England) in an effort to attract and retain talent.

However, a recent BICS survey shows 28 per cent of businesses surveyed cannot afford to offer enticing pay packages to applicants, most notably within the hospitality industry, where 51 per cent of those surveyed reported this issue. This suggests businesses, especially those in industries most affected by the various social restrictions over the past two years, will continue to struggle to fill their vacancies until the threat of Covid-19 is consistently low enough for these businesses to build up appropriate cash reserves and match the wage demand of new hires.

In November, growth in nominal earnings was 3.8 per cent, continuing a downward trend as base effects from the period of the CJRS continue to dissipate. Inflation, on the other hand, is trending in the opposite direction, with CPI rising to 5.4 per cent in December. This real pay squeeze will continue throughout 2022, as the Bank of England expects CPI to peak at over seven per cent by spring.

On top of this, April will see the 1.25 percentage point rise in National Insurance contributions, alongside an expected 54 per cent rise in gas and electricity bills for the typical household following the revision to Ofgem's energy price cap. To offset some of the latter pressure on households, government will introduce a combination of support through lower council tax bills and loans to reduce the immediate hit of the prices increase, phased in over the course of this year.

Overall, it is not good news for household budgets in 2022: the Bank forecasts real household disposable income will fall by two per cent this year. This is the largest drop in spending power since at least 1990; NIESR predicts this will most negatively affect lowest-income households largely concentrated in the North West, Wales and parts of the South East.

Declining confidence over household finances contributed to lower consumer sentiment in January. According to GfK, consumer confidence fell further as confidence about the general economic situation in the coming 12 months declined. It is clear households are bracing for the increasing costs of living coming in the next quarter, which has further translated into a fall in the major purchase index, measuring consumers' willingness to buy expensive items.

This has contributed to the Bank of England revising down its forecasts for GDP in 2022 as global energy and tradable goods prices rises weigh on aggregate spending. Attention should also be paid to UK trade in the coming year, with increased trade barriers between the UK and EU through increased goods checks, due to the next phase of Brexit, providing further hindrance to domestic growth.

Despite the more subdued growth outlook, the Bank Rate rose to 0.5 per cent in February in reaction to rising global energy and tradeable goods prices. Four out of the nine Monetary Policy Committee members voted for a rise to 0.75 per cent. Such a close decision explains many economists' expectations that we will see further increases to the costs of borrowing for UK households in the near future.

Altogether, despite Omicron leaving little lasting effect, there are clearly challenges ahead for many UK households in 2022. Preparation for the incoming rise to costs of living can be seen through declining consumer confidence, with expected real wage decreases likely further squeezing household budgets throughout the year.

Consumer spending: card spending close to pre-pandemic trends, despite Q4 dip

Consumer confidence dropped away somewhat in Q4, as the rapid spread of the Omicron variant added to households' uncertainty, both about their own position and the wider economic situation.

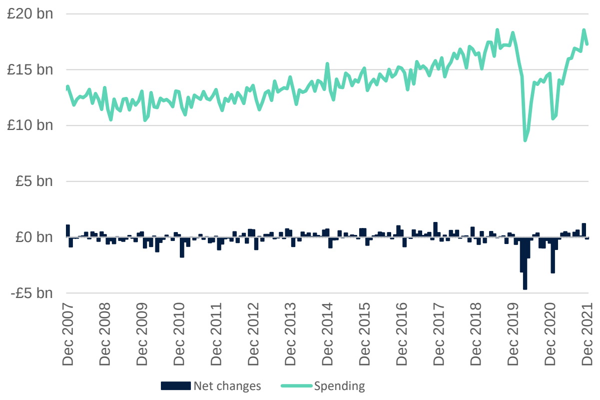
Despite this, card spending continued its recovery back towards the pre-Covid 19 trend. There was a solid pick up in spending in November, boosted by black Friday sales and pre-Christmas spending. In addition, the increase in the contactless limit may also have provided an additional boost.

Anecdotally, growing levels of spending using Buy Now Pay Later services (not included in card spending figures) will mask a higher level of total spend. However, with consumer sentiment the main driver of activity, the overall trend is likely to echo that for cards.

However, there was a modest decline in activity in December. Given this was concentrated in the services sector, this is likely a reflection of increased caution and behaviour change amongst consumers with respect to social activities in light of the new Omicron variant.

Notwithstanding this, card spending now appears to be approaching its pre-Covid 19 trend path (***Chart 1***).

Chart 1: Credit card spending in month



Source: UK Finance

With the economy now effectively fully open, the remaining gap between current spending levels and those seen before 2020 may take longer to close, as consumer demand in some sectors experiencing more persistent impacts of the pandemic may settle on a lower level. Commuting costs, for example, are lower for many consumers because of more flexible working arrangements, which in some cases have now morphed into long-term employment policies.

Linked to this, related spend in and around business centres – including food, drink and entertainment – may not recover to former trends, although this will be at least partly offset through substituted spending where those workers live.

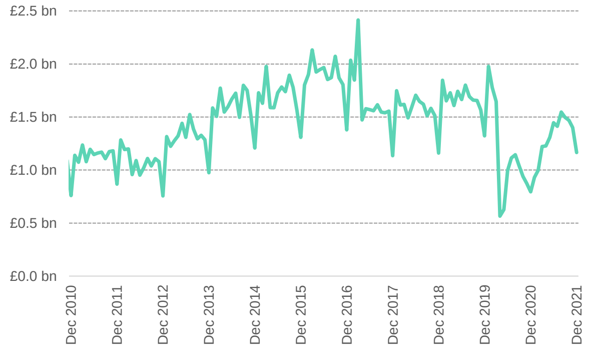
Consumer spending: personal loan demand also nearing pre-Covid-19 levels

Personal loan borrowing (which excludes car finance) followed a similar pattern to that seen for credit card spending (***Chart 2***), although the drop off in activity was somewhat more pronounced. Recovery in demand for loans in mid-2021 was likely partly driven by the surge in home improvement activity, with personal loan borrowing for associated larger purchases seeing a related boost.

There is clearly a degree of seasonality with new loans generally declining at the end of the year. Emergent concerns about rising inflation and upcoming cost of living pressures further weighed on demand for loans in the latter part of 2020.

While our data does not specifically cover finance for car purchase, insights from the Finance and Leasing Association point to a recovery in finance for car purchase, particularly used cars, in the latter part of 2021 though volumes remain down on pre-Covid-19 levels.

Chart 2: Amounts of new personal loans from banks



Source: UK Finance

Looking ahead, spending in a number of areas is likely to see growth in cash terms from the rising cost of living, and so figures need to be interpreted against this inflationary backdrop.

It remains be seen how the squeeze on household finances will impact on spending patterns through the year. However, it is likely that for some consumers, particularly at the lower end of the income scale, the ability and desire to make larger purchases will be more constrained. This could then bear down on personal loan borrowing and, to a lesser extent, card spending.

2021 – a record breaking year for the housing market

With full year data now available, we can look back on 2021 as a quite remarkable, expectation-busting, year for housing and mortgage markets.

Although a normal review of the year's outturns would involve comparisons with the previous year, the huge disruptions through both 2020 and 2021 mean that it is also revealing to compare with 2019, the last year of the "old normal" before Covid-19 fundamentally changed the ways we live, work, and spend.

Firstly – and most obviously – house purchase activity saw an unprecedented boom, fuelled both by Covid-19 triggered social change and the Stamp Duty holiday. On the back of these multiple stimuli, the number of loans to buy property increased by 41 per cent overall (***Table 1***).

Table 1: Key mortgage figures, 2019-2021

	2019	2020	2021	Annual change
Number of house purchase loans:				
First-time buyers	351,000	304,000	405,000	33.2%
Homemovers	344,000	310,000	442,000	42.6%
Buy-to-let landlords	75,100	66,600	111,600	67.6%
Total	770,100	680,600	958,600	40.8%
Number of mortgage refinances				
Residential - external remortgage	446,400	352,400	286,800	-18.6%
Residential Product Transfers	1,203,200	1,169,100	1,253,700	7.2%
Buy-to-let external remortgage	189,400	164,500	153,600	-6.6%
House Prices (UK average, Q4)	215,925	229,819	253,113	10.1%
Gross mortgage lending (£ million)	269,006	245,716	313,158	27.4%
Mortgages in arrear (end of year)	80,570	89,310	85,650	-4.1%
Mortgage possessions	7,990	2,620	2,250	-14.1%

Source: UK Finance, Nationwide BS, Bank of England

While this growth is unprecedented in the mortgage market, it needs to be taken in the context of the suppressed volumes in 2020 for the periods when the housing markets were disrupted amid wider social distancing restrictions. The strong annual growth in 2021 therefore partly reflects delayed activity from the previous year.

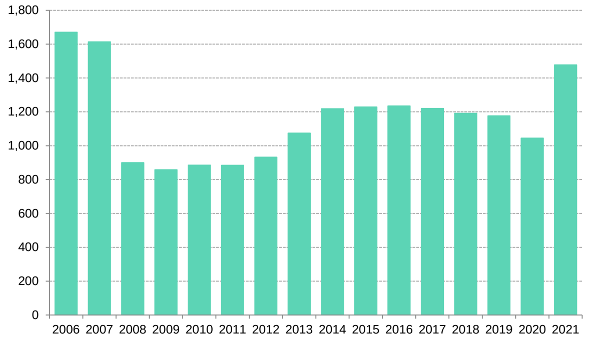
However, beyond this, the Stamp Duty holiday provided considerable additional stimulus to purchase markets; as we have observed previously, the strongest drivers of purchase lending growth throughout the past two years have been homemover and buy-to-let lending, with these borrowers benefiting most from the Stamp Duty holiday.

Finally, the changing work patterns and lifestyle preferences brought about by the pandemic have introduced a further boost to demand for housing outside UK cities and their traditional commuter belts.

With activity levels boosted by all these factors, house prices saw very strong growth in 2021 as demand outstripped the supply of homes up for sale. According to the Nationwide Building Society, house prices finished 2021 up ten per cent on 2020, the strongest price growth since 2004.

As shown in ***Chart 3,*** property transactions – the key indicator of overall housing market activity including both mortgage and cash purchases – totalled a little under 1.5 million in 2021, considerably more than making up for the ground lost in 2020 from the temporary closure of UK housing markets and other Covid-19 related impacts. In fact, 2021 was, by some distance, the strongest year of housing market activity seen since 2007, just before the Global Financial Crisis (GFC).

Chart 3: Property transactions, UK



Source: HM Revenue and Customs

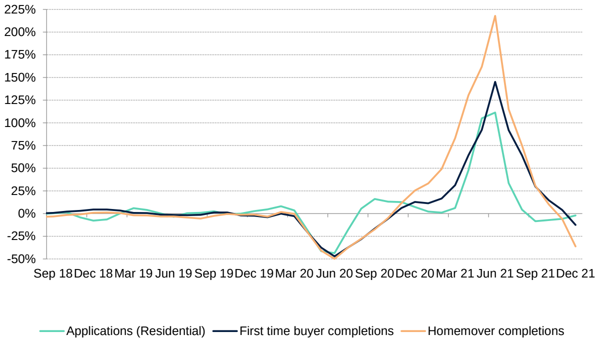
Meanwhile, helped by government and industry support for incomes and payments, the number of borrowers in payment difficulties fell, contrary to expectations before the year began.

Having risen only slightly in 2020, with payment deferrals helping millions of borrowers who had been affected by the spread of Covid-19, mortgage arrears fell back in 2021, and the year-end position was close to the record lows seen just before the pandemic struck.

House purchase activity fell away in Q4 2021

House purchase activity dropped sharply in Q4 2021, which was entirely expected following the end of the final phase of the Stamp Duty holiday in September (***Chart 4***).

Chart 4: Mortgage applications and completions, 3-month moving average, year-on-year change



Source: UK Finance

However, the drop off was somewhat lower than that seen following previous Stamp Duty rate changes, for example when the surcharge on additional property was brought in in 2016.

Overall, homemover activity was 36 per cent down year on year, and first-time buyers down 12 per cent – the smaller drop-off for the latter reflecting the lower growth seen previously. That compares with a 47 per cent annual contraction in BTL purchase activity in Q2 2016 when the surcharge came into effect.

This is notable because Q4 2020, boosted by the factors described above, was itself significantly above levels seen in the final quarter in any year since 2007.

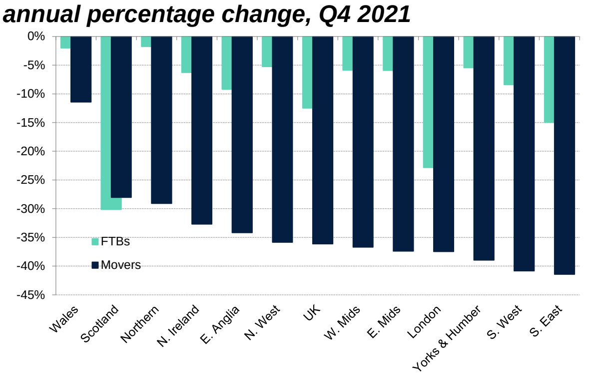
Bearing in mind that Q4 2021 was the first quarter that the Stamp Duty holiday was no longer in place, this supports our observation (in our Q3 2021 Review) that the societal changes stimulating housing market activity in the Covid-19 era are yet to fade.

Looking ahead, applications data for Q4 2021 suggests that, although activity in Q1 2022 is likely to be lower than in Q1 2021, the drop off again is likely to be relatively modest, and levels will remain strong compared with the trends seen in the years leading up to the pandemic.

Post-Stamp Duty drop off in lending strongest in the "new commuter belt"

The expected post-Stamp Duty holiday contraction in lending in Q4 2021 was seen across every region of the UK, with the contraction significantly greater for homemover activity than for FTBs everywhere barring Scotland (***Chart 5***).

Chart 5: Number of new house purchase loans, annual percentage change, Q4 2021



Source: UK Finance

This too is entirely expected; having disproportionately benefited from the Stamp Duty holiday, homemover numbers saw far stronger growth whilst it was in place, and so the subsequent adjustment following the end of the holiday was commensurately greater.

In Scotland, the trend again reflected the pattern of growth last year, with the differing regime for Land and Buildings Transactions Tax (LBTT – the Scottish counterpart to Stamp Duty) meaning that FTBs saw proportionately more benefit from the purchase duty holiday in place there than elsewhere in the UK.

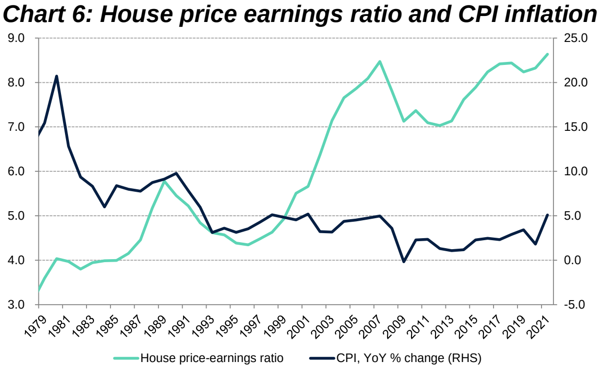
The greatest contraction was seen in the South East and South West, with these regions having seen some of the strongest growth figures over the previous year, driven in large part from homeowners looking to move (or buy additional property) further away from London and the traditional commuter belt.

New mortgage affordability facing pressure from rising inflation

Last year, against a backdrop of a housing market turbocharged by social change and taxation stimuli, UK house price growth rose by over ten per cent, far outstripping wage growth.

As a result, the house price-income ratio in 2021 rose to record levels, beyond even the peak levels seen in the boom years those seen just before the Global Financial Crisis (GFC) (***Chart 6***).

Chart 6: House price earnings ratio and CPI inflation



Source: Office for National Statistics, HM Land Registry

However, at the turn of the previous market cycle inflation plunged sharply as the credit crunch took hold. The subsequent growth in house prices since the recovery, from around 2009, was against a backdrop of low inflation, averaging around two per cent.

In contrast, CPI inflation rose to over five per cent in the latter part of 2021 and is now expected to rise further to over seven per cent this year.

As prices rise through the year, this will weigh more heavily on household balance sheets, particularly amongst lower-income households who spend proportionately more of their income on essential items, including energy and food, both of which are seeing particularly pronounced cost increases. An additional pressure will come from increased National Insurance contributions from April.

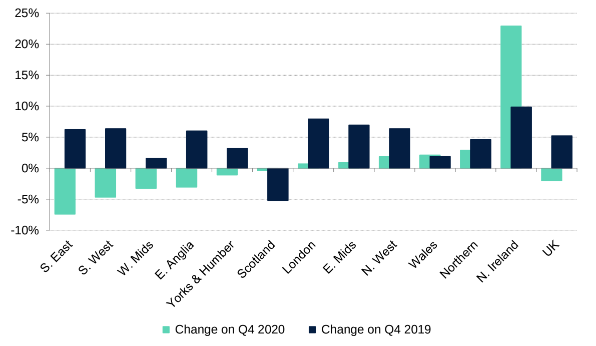
Combined with this, the increased cost of funds for lenders from Bank Rate rises in December and February (and market expectations of more to come to keep inflation in check) will place upward pressure on new mortgage lending rates. However, the current volatility in money and bond markets makes the precise path of longer-term rates hard to predict.

All of these factors will have an impact on the income-expenditure affordability tests that form part of the FCA rules on responsible lending, in place since 2014. This will bear down on effective demand and therefore on new lending, particularly at the lower-income end of the market. However, these affordability rules ensure that those taking out a mortgage now have a good degree of resilience in the face of growing household cost pressures.

Q1 activity set to soften but still in growth territory – even compared to pre-COVID era

Looking ahead, UK Finance data on mortgage applications indicate that lending will move back towards growth territory in early 2022, following the post Stamp Duty holiday drop-off seen in Q4 2021. Overall, there were two per cent fewer mortgage applications submitted in Q4 2021 than in the same quarter a year previously (***Chart 7***).

Chart 7: Residential mortgage applications, Q4 2021, change on one and two years ago



Source: UK Finance

As observed above, this is noteworthy, given the elevated levels seen a year previously, and would represent healthy growth compared with pre-pandemic levels.

Growth rates varied widely across regions, with the southern English regions outside the capital all pointing towards a modest annual contraction in Q1 2022, whilst most other geographies look likely to return to annual growth. All regions of the country, barring Scotland, look set to show growth in lending compared with pre-pandemic levels.

Consumer spending and lending: summary

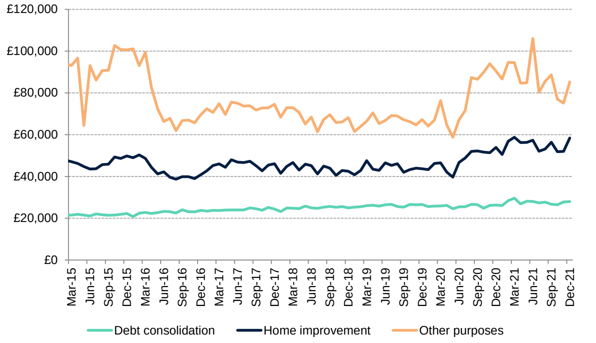
Q4 2021 saw a contraction in spending patterns off the back of an Omicron-driven wobble in consumer confidence. Meanwhile mortgage lending saw the expected post-Stamp Duty holiday decline, but signs are that other Covid-19 era demand stimuli linked to changing living and working patterns have not yet run their course.

The paths for consumer spending and borrowing over the coming months are both dependent on how households cope with the inflationary pressures now in the system, with the potential for this to add to the "K-shaped recovery," as lower-income household finances are disproportionately impacted.

Household refinancing: boom in extra borrowing starting to abate

The surge in equity withdrawal when remortgaging to fund additional property purchase, which we have observed in previous Reviews, appears to be tailing off following the end of the Stamp Duty holiday. Although the amounts withdrawn for "other reasons" are still significantly up on pre-pandemic levels, this now appears to be following a downward, if erratic, path (***Chart 8***).

Chart 8: Average value of equity withdrawal through residential remortgages



Source: UK Finance

This is intuitive, with the tax break stimulus to acquire additional property wealth (whether for rental or occupation) no longer in place.

However, the second equity withdrawal feature seen through the pandemic, namely significantly increased sums withdrawn for home improvements, is proving more persistent.

This is likely to reflect the continuing move towards creating better living and homeworking spaces in a world where these spaces have become far more important.

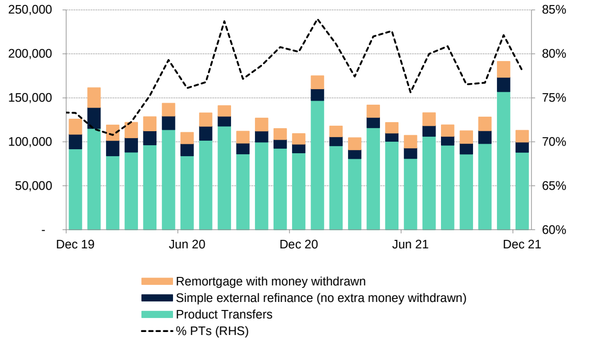
However, it also reflects the inflationary pressures on carrying out this work, with construction sector labour and materials costs elevated even in the early months of 2021, well before the wider inflationary environment we are currently seeing.

Stripping out these inflationary pressures, this is further evidence of a housing market that has evolved to reflect work and life choices in a world reshaped by Covid-19, possibly for the long term.

Household refinancing: product transfers dominate for now

Refinancing overall in Q4 2021 continued to follow the pattern of maturing fixed rates, with a particular spike in November, seen across both internal Product Transfers (PTs) and external remortgage (***Chart 9***).

Chart 9: Number of residential remortgages and internal product transfers



Source: UK Finance

Although each lender's own maturity profile varies according to business plans and popularity of their mortgage products in previous years, this timing does coincide with an increase in popularity of five-year fixed rate mortgages some five years ago.

This trend is set to increase through this year and into 2023, as we highlighted in our Mortgage Market Forecasts in December, reflecting the increased popularity of longer-term fixed rates in the final years of the last decade.

Household saving: deposits continue to grow but modest signs of slowing

Since the onset of the pandemic retail deposits have seen elevated growth, compared with that seen previously, as social distancing restrictions limited spending in some sectors.

Throughout 2021, as almost all restrictions were progressively lifted, the rate of increase in household deposits eased, but was still higher that that seen prior to 2020, as spending on some activities, including commuting travel costs, remained suppressed.

Q4 2021 saw this continue, with total deposits rising to a little under £1.1 trillion. The increase was concentrated entirely within instant access accounts, while time deposits continued to decline in the face of negative real rates of return, even for longer-term savings products.

With interest rates increasing (and expected to rise further over this year) we may see some growth in demand for longer-term savings products. However, while nominal rates remain well below inflation, this is likely to be limited in scope.

Household refinancing and savings: summary

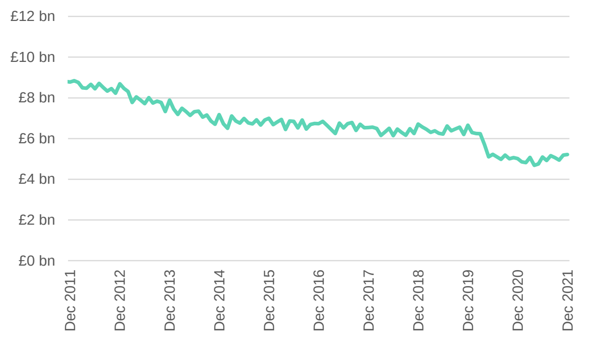
Refinancing activity overall continues with little regard to the Covid-19 impacts that have so fundamentally changed borrowing for house purchase. However, the equity withdrawal element of remortgaging has changed almost as dramatically, with amounts withdrawn increasing rapidly.

With the end of the Stamp Duty holiday, remortgage borrowing to fund additional property purchase looks to be falling away but changing patterns of living and working have led to more borrowing for home improvements. This this looks set to continue for now, as more homeowners take the opportunity to adapt their property to suit their needs.

Household debt: overdraft balances start to rise

In the early months of the pandemic, overdrafts levels fell sharply, with many monthly outgoings reduced or suspended during lockdowns. Mirroring the patterns in spending, overdrafts started to increase (albeit slowly) through 2021, and this continued in the final quarter (***Chart 10***).

Chart 10: Overdraft balances outstanding



Source: UK Finance

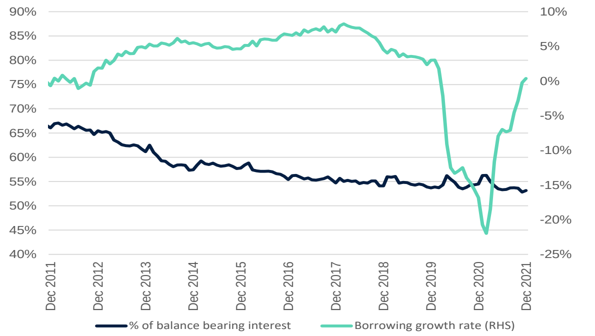
Despite these rises, overdraft utilisation remains significantly below pre-pandemic levels, an indication that cost-of-living pressures have yet to make a material impact on the ability of monthly incomes to cover monthly household outgoings.

However, as an indicator of household payment stress, should this begin to increase more rapidly this may be an important early sign that the cost of living has begun to bite in a more significant way.

Household debt: credit card debt increasingly paid off each month

Overall, growth in outstanding credit card debt moved into positive territory for the first time since the onset of the pandemic. The sharp decline in outstanding balances in early 2020 was triggered by the reduction in spending opportunities and repayments outstripping card borrowing. Although the growth rate is still currently considerably lower than just before the pandemic, this had already been on a downward trend since 2017 (***Chart 11***).

Chart 11: Credit card balances outstanding



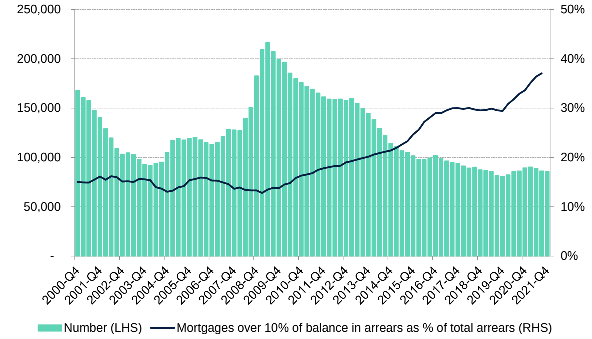
Source: UK Finance

However, when looking at potential indicators of household stress a more important metric is the proportion of card balances that are interest-bearing, meaning that they have not been fully paid off each month. As Chart 11 shows, barring two temporary spikes corresponding to the two periods of lockdown (when opportunities for spending were restricted and, at the same time, the Payment Deferral scheme allowed borrowers to delay payment without penalty) this metric has been trending down throughout the pandemic era and this continued in the final quarter of 2021. Again, then, unsecured borrowing data gives no sign as yet of any early pressure on household finances, either in response to rising consumer prices or from any post CJRS impacts on employment and wages.

Household debt: mortgage arrears in good shape as cost-of-living pressures loom

Arrears overall continued to fall in Q4 2021, continuing the trend seen through the whole of 2021 (***Chart 12***). Importantly, this was the first arrears data since the end of the CJRS on 30 September, with the mortgage Payment Deferral scheme having concluded fully two months before that.

Chart 12: 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

Although reportable arrears take some time to build up it is encouraging that, following the end of this support, there was no immediate increase in borrowers unable to meet their monthly mortgage payments, having held arrears at bay with the help of that temporary support from industry and government.

Within the downward trend for overall arrears numbers, we have seen the number of customers in deeper arrears, who already had significant payment shortfalls before the pandemic struck, continue to increase. The possessions moratorium, and subsequently the restricted capacity of the courts, has meant many borrowers in unrecoverable arrears positions - who would normally have exited their mortgage by this stage through possession - have instead seen their positions worsen.

This increasing stock of heavy arrears cases will gradually ease over the course of 2022 into 2023, as the backlog of delayed possessions is cleared.

With the labour market situation following the closure of the CJRS now becoming clearer, forecasters are now expecting only a modest rise in unemployment. However, while unemployment is likely to be a lower risk to arrears than previously anticipated, inflation is emerging as a more significant threat to household balance sheets and, within this, mortgage payments.

As inflation continues to outstrip wage growth through this year, and additional National Insurance contributions kick in from April, real disposable household incomes will be increasingly squeezed.

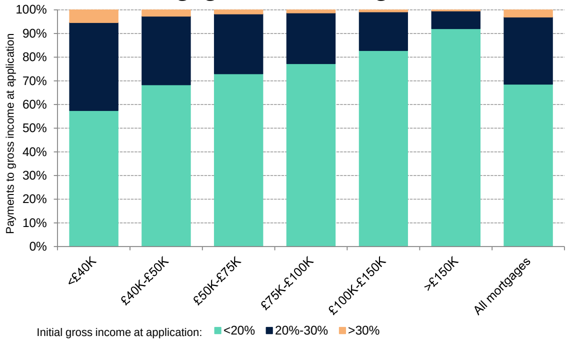
Rate rises in response to inflation will also add to the payment burden for those customers on variable rates, although the three quarters of borrowers currently on fixed-rate deals will see no immediate impact.

As we have observed in previous Reviews, variable rate borrowers typically have significantly lower balances than those on fixed rates and so will see a relatively small increase in payments in absolute terms. However, the two rate rises since December, as well as any more to come as the Bank of England moves to control inflation, will incrementally add further pressure on these households' ability to meet all their monthly outgoings.

Overall, although we expect arrears to increase, the responsible lending rules in place since 2014 ensure that borrowers have a buffer against adverse rate and income shocks such as these, and this will greatly help moderate the extent of increases in arrears.

Helped in large part by this prudent underwriting, our data indicate that some 70 per cent of current residential borrowers needed less than 20 per cent of gross income to meet total mortgage payments (at the time of application), and almost all needed under 30 percent (***Chart 13***).

Chart 13: Proportion of income needed to meet initial mortgage payments, by income at origination, residential mortgages outstanding



Source: UK Finance

Notes: 1. Income and payments measured at application; data on current income are not available

This points to a sizeable majority proportion of income left over after mortgage payments for the vast majority of mortgage customers. This provides borrowers significant room to flex other outgoings, as they typically prioritise payments on their home above other outgoings.

However, it should be noted that, within lower income brackets, a higher proportion of borrowers have less room to manoeuvre. Again, this suggests that, at the margins, inflation is likely to place pressure on arrears numbers, particularly amongst lower-income households.

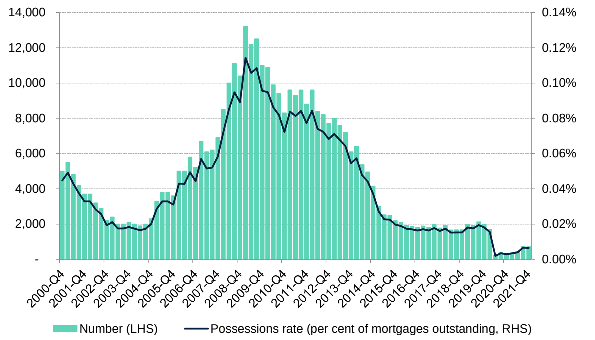
Household debt: possessions activity increases gradually

Following the end of the possessions moratorium in early 2021, possessions started to increase. However, the restricted court capacity has limited the number of cases that could be dealt with.

Possessions remained at historically low levels in Q4 2021, with activity further suppressed by the voluntary industry moratorium on possessions activity over the festive season.

As a result, possessions numbers remained far lower throughout 2021 than we would normally see, even at the lowest point in the possessions cycle. For example, at the lowest point in the early 2000s there were 8,200 annual possessions. Last year saw a total 2,250 mortgage possessions, just over one quarter of that previous low (***Chart 14***).

Chart 14: Number and proportion of 1st charge mortgages taken into possession in period



Source: UK Finance

Although we expect possessions to rise from these abnormally low levels, the anticipated increase the next two years would only see figures rise to levels we last saw in the ***low*** point of the previous cycle.

It is also important to reiterate that the possessions carried out last year, as well as those expected in 2022, relate to cases which were already in possession proceedings at the start of 2020.

With new arrears cases on a downward trend, this eases the potential pressure on an already-overloaded court system as it works with lenders to clear the backlog.

While there will inevitably be new cases where borrowers, unfortunately, do not recover their position and eventually proceed to possession, the help provided by government and the industry to contain payment problems will mean that such cases, if and when they emerge, will not place pressure on the system through this year.

Household debt: Summary

In the final quarter of 2021, we saw no signs of increasing household payment stress, even with all Covid-19 specific support measures having ended. In fact, arrears continued to tick down, and unsecured debt levels and payments give no early indication of stress at this stage.

While unemployment now appears to have faded as a risk to arrears, the looming pressure due to cost-of-living increases is of more concern. However, with arrears near record lows and most mortgage borrowers having a good measure of flex in their household budgets, we expect a modest rise in borrowers unable to meet their monthly payments.

While possessions will rise this year, this relates to cases which would normally have been resolved some time ago and now need to be concluded in the best interests of the borrower, with all other avenues to repay arrears exhausted.

As always, any customers facing difficulty meeting their mortgage or other credit commitments are encouraged to talk to their lender at an early stage, as the industry stands ready to help with a range of forbearance tools.

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