Intermediary Mortgage Lenders Association – 2022 manifesto

Despite – and in some cases as a result of – the continuing COVID-19 pandemic, 2021 remained a very busy year for the housing market. The experience of "lock-down" prompted some homeowners to relocate out of city areas in search of more space and greener surroundings. The extension of the Stamp Duty holiday to September kept demand high amongst home buyers and landlords. Even after that incentive was withdrawn, the sector remained busy, with the first of a possible series of rate rises from the Bank of England set to drive re-mortgaging business in the immediate future.

Amid this ongoing demand, there is still plenty for the sector to get to grips with as we enter 2022. Our latest manifesto identifies the key areas that we believe should be a focus for the mortgage market and the Government in the year ahead.

Summary

1. Housing supply and affordability

The imbalance between supply and demand in the UK housing market continues to keep property prices high. We remain convinced of the long-term financial benefits of home ownership – and this is underpinned by regular surveys which indicate that a majority of people do see home ownership as something to which they aspire. The British Social Attitudes Survey of 2018 reported that 87% of those surveyed would prefer to buy rather than rent – a proportion which has changed little over the previous 30 years.

The future of Help to Buy and continued support for low-deposit borrowers

First-time buyers looking to find cash deposits of 5% will continue to struggle unless assisted by family or specific schemes designed to help them. The industry has already launched a number of initiatives to take the place of the Government's Help to Buy scheme, which is due to be withdrawn at the end of March 2023. It is not IMLA's role to endorse or promote specific schemes – but we are happy to help keep members informed about new developments in the market.

First Homes

The First Homes scheme was announced in May 2021 and Phase 1 of the pilot projects is about to go live. It is still relatively small-scale and its success will ultimately depend on the appetite of developers to get involved and self-fund the initiative. We have expressed some concerns about how borrowers using the scheme to buy their first property would be able to trade up in the future, given the requirement to sell at a 30% discount.

Affordability and stress testing

We understand the importance of protecting borrowers from over-extending themselves: however, the current approach to affordability means that borrowers are often being tested at completely unrealistic rates. We have consistently argued that the combination of the FCA's affordability rules and the Financial Policy Committee's additional stress test of 3% above SVR has prevented numerous prospective borrowers, including many first-time buyers, from stepping onto or up the housing ladder. We therefore welcome the news (announced on 13th December) that the Bank of England is to consult on removing the 3% stress test.

2. Serving non-standard customers

Our membership has always included a number of specialist mortgage lenders – and many of our "mainstream" members also offer a range of products for applicants who do not fit traditional "mainstream" criteria. This year we surveyed consumers and members to find out more about perceptions of what may and may not be possible. The results were very positive – we believe that many consumers would be able to find a mortgage to suit them if they were to approach an expert mortgage intermediary to advise them on what is available in the market. The over-riding message is – you may not be eligible for the lowest rates advertised, but that does not mean that you will not be able to get a mortgage. We will continue to emphasise this message and work with our intermediary colleagues to reach as many aspiring homeowners as possible.

3. The Green agenda – improving domestic energy efficiency – we accept that the domestic property market must play its part in helping to achieve net-zero carbon emissions by 2050. But proposals for obliging property owners to carry out improvement works must be carefully thought-through and subject to strict quality controls if limited resources – both materials and cash – are not to be wasted. We also believe that EPCs – on which so much reliance is currently being placed – need to be closely examined and assessed to ensure they are fit for purpose. There is a danger that piecemeal policy will lead to confusion and a variety of unintended consequences: the task is immense but the Government must lead in co-ordinating a strategy for planning, incentivising and funding work to improve the energy efficiency of Britain's housing stock.

4. The Buy-to-Let market

Britain's private rented sector is an essential component of the housing market, providing homes for one in five (20%) UK households. The sector has remained vibrant despite a 'layering' of policy changes introduced by previous administrations, but there could be more unwelcome measures in store, such as proposals to increase Capital Gains Tax rates to mirror income tax. IMLA has consistently argued that the Government should resist making additional changes that may deter landlords from further investing in the Buy to Let market, as this could lead to significant numbers exiting the sector. This will only push rents up – making the tenure more expensive for all tenants, and leaving those who are trying to save for deposits with less disposable income and thus less able to do so.

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1. Housing supply and affordability

1.1 The UK's housing market continues to be underpinned by the simple economics of supply and demand: we are not building enough new homes to meet consumer demand – whether from owner-occupiers or those who want or need to rent. Successive Governments have announced schemes which promise to deliver the magic figure of 300,000 new homes every year – and as each scheme falls short of this target, the cumulative shortfall grows.

1.2 The current Government has tried to address this by looking at simplifying and speeding up the planning process, enabling more homes to be built faster. In the last couple of years, the pressure on supply of building materials, the loss of skilled foreign labour and the impact of the covid lock-downs have all added to the challenges. Going forward, we have the added challenge of ensuring that all new-build meets stringent standards of energy-efficiency.

1.3 The most obvious result of demand outstripping supply is the high price of residential property in the UK. According to the Office for National Statistics, the average price of a home in the UK in November 2021 was £270,000. With average salaries estimated to be anywhere between £26,000 and £31,000, this is clearly beyond the reach of many aspiring homeowners. So first-time buyers need to start small, with properties which are below the average price, and be prepared to save hard for a deposit of at least 5%. If they are able to secure a 95% mortgage, then repayments should be relatively affordable given the continuing low interest rate environment. But many first-time buyers will need more help – many from the Bank of Mum and Dad - or other specific schemes.

The future of Help to Buy and continued support for low-deposit borrowers

1.4 IMLA has frequently commented on the fact that a large cohort of individuals who might normally be expected to have become property owners have not done so – and that, in the long-term, this is likely to have a detrimental effect on their finances. Two of our research reports in particular – *The Intergenerational Divide in the Housing and Mortgage Markets* (October 2019) and *The Mortgage Affordability Paradox* (November 2021) – highlighted this issue, with the latter noting that since 2007 a cumulative shortfall of 2.7 million first time buyers has arisen with 2020 seeing a shortfall of nearly 200,000 compared to the expected total based on previous propensities to buy.

1.5 One of the major barriers to new home purchase is the cost of housing, and the cash value of deposit required. Since its introduction in 2013, the Government's Help to Buy (HTB) scheme has helped over 420,000 households into homeownership, with a further 1.2 million individuals opening HTB ISA accounts offering Government bonuses of up to £3,000 on top of savings that can be put towards a deposit. HTB was never intended to be permanent, however, and will be withdrawn completely at the end of March 2023. Given the lead-times for building new homes, a significant number of properties likely to be sold under the scheme will already be under construction and reserved. There is therefore an immediate need for alternative schemes to help first-time buyers.

1.6 The Government launched its own Government's Mortgage Guarantee Scheme in March 2021. With a relatively short lifetime – it is due to run until the end of 2022 – this scheme also has limitations in that its terms of engagement prevent participating lenders from committing to other schemes whilst it is operational. But the fact that the Government has been prepared to back higher LTV lending has undoubtedly encouraged other lenders back into the high LTV space – ideally on a longer-term basis.

1.7 Over the past few years the industry, aware that the days of HTB are numbered, has been working on developing a variety of alternative schemes – and some of these have now been successfully launched. From lenders' perspective, it is important that schemes are sustainable and do not impose complex conditions or restrictions. Clearly it is a matter for each individual lender to decide whether to engage with a particular scheme – and IMLA does not endorse any specific initiative. We are happy to help keep members informed about new developments, however.

First Homes

1.8 The First Homes scheme was announced in May 2021 and Phase 1 of the pilot projects is about to go live. To qualify, properties must be discounted by a minimum of the market value and the first sale price must be no more than £250,000, or £420,000 in Greater London. Purchasers must have a combined annual household income not exceeding £80,000 and, when selling the property, must do so at a 30% discount of the market value.

1.9 The success of the scheme will ultimately depend on the willingness of developers to get involved and self-fund the initiative. We have also expressed some concern about whether borrowers who use the scheme to purchase their first property will be able to trade up in the future, given the requirement to sell at a 30% discount. It may take some time for borrowers to be able to build up sufficient equity to save a large enough deposit to buy a larger property. But, by definition, "First Homes" will be designed to be just that – and will not be large enough to accommodate growing families.

Affordability and stress testing

1.10 We have consistently argued that the combination of the FCA's affordability rules and the additional Financial Policy Committee (FPC) stress test of 3% above a Standard Variable Rate (SVR) has prevented numerous prospective borrowers, including many first-time buyers, from stepping onto the housing ladder. Moreover, the fact that this 3% stress test is not required in relation to loans that are fixed for five years or more could be causing some market distortions.

1.11 Our recent report *(The Mortgage Affordability Paradox)* highlighted the stress test as one of the major contributors towards the low numbers of first-time buyers between 2008 and 2020, averaging just 270,000 a year.[1] Addressing this barrier would help to bring the actual affordability tests which lenders – quite reasonably – need to carry out before approving loans, much more into line with what borrowers can expect and afford to pay.

1.12 When the Bank of England decided in December to raise the Bank lending rate to 0.25%, many commentators pointed out that the effect on mortgage payers would be relatively small, given that approximately 75% are locked into fixed-rate deals. First-time buyers can similarly expect to be offered deals which are fixed or discounted – and thus lower than the SVR. Whilst there may be some logic in stress-testing whether a borrower would be able to sustain repayments at the lender's reversion rate (which will generally be the SVR) – to add a further 3% stress on top is unrealistic given that the vast majority of borrowers can expect to be able to re-finance a fixed-rate deal when it comes to an end – at a rate which is lower than lender's SVR. The additional 3% is also excessive given the expectations of where the Bank rate may be in a few years' time: although inflation may rise to 5% and above, it seems very unlikely that the Bank would increase the lending rate to that level. We therefore welcome the announcement that the Bank of England is to consult in 2022 on removing the 3% stress test.

2. Serving non-standard customers

2.1 Even before the pandemic struck, the UK had a number of specialist lenders whose main focus is to design products for borrowers whose individual circumstances do not meet the "mainstream" criteria applied by many high-volume lenders. Many of those mainstream lenders also offer specific products to targeted groups of applicants – and are able to apply more bespoke underwriting and assessment procedures to ensure that loans are always suitable for the borrowers and responsibly approved.

2.2 The pandemic affected different groups of people in different ways – the self-employed and those in the hospitality and entertainment sectors were particularly hit, as were many who work on contracts and/or previously had several sources of income, some of which dried up. Research

[1] http://www.imla.org.uk/resources/publications/the-mortgage-affordability-paradox-rob-thomas-imla.pdf

undertaken in the second half of the year showed that a number of people who would like to apply for a mortgage have been deterred from doing so because they think they would not be eligible. This may be true for some – but there will be many who would qualify – if they knew where to go to find out more.

2.3 We published the results of our research in a report called *Why under-served borrowers should not rule themselves out*. We shall continue to focus on the message to individual borrowers – which is that while they may not be eligible for the cheapest deals available, that does not mean that they will not be able to get a mortgage. Expert mortgage intermediaries are there to help them identify the right deal at the right price.

3. The green agenda – improving domestic energy efficiency

3.1 Ambitious net-zero targets have pushed the Government to consider what action it must take to reduce the emissions created by housing in the UK. In addition, the build-up to the COP26 conference in November galvanised many more consumers to be pro-active in their demands for Government and industry to do more to tackle climate change.

3.2 The mortgage market clearly has a role to play in the path to net-zero and this year we have seen a number of initiatives from lenders and proposals put forward by the Government to create a greener market. Over the past 15 months the Department for Business, Energy and Industrial Strategy (BEIS) has undertaken two consultations. The first, in September 2020, proposed that the EPC rating of all privately rented homes should be raised to Band C for new tenancies from 2025 and all tenancies from 2028. The second, in February 2021, included a proposal that lenders should collate information on the EPC ratings of all properties on their mortgage book and aim to achieve an "average" rating of Band C. We have expressed concern about the potential impact which these requirements could have on the mortgage market and private rented sector.

3.3 First, the requirements could impose a significant financial burden on landlords. Currently all rented property must be rated at least Band E unless exempt - and the cost of improving energy efficiency is currently capped at £3,500. Under the BEIS proposals that cash limit will rise to £10,000, although the Government estimates that the average cost of bringing properties up from Band E or D to Band C would be around £4,700. Landlords are encouraged to apply for the Green Homes Grant, which will fund at least two-thirds of the cost, up to a limit of £5,000.

3.4 Second, we believe that if too much emphasis is placed on lenders being 'encouraged' (or potentially required) to ensure their books achieve a target average EPC rating, there is a risk that some may limit borrowing on lower-rated, less efficient properties. This could potentially create a new group of mortgage prisoners – those who live in poorly-rated housing but who can neither afford to improve the building's efficiency nor re-mortgage. There may be scope for incentivising lenders to help homeowners borrow in order to fund essential improvements.

3.5 We have also warned that steps must be taken to ensure that contractors carrying out improvement works are properly qualified and regulated – and that the work done is to an acceptable and approved standard. There is a real danger of creating a "cowboys' charter" and allowing a lot of sub-standard and possibly unsafe work to be carried out – only to be removed and replaced at greater cost. We need to use our limited resources – both materials and finances – wisely and effectively.

3.6 BEIS has yet to report back its conclusions from these two consultations and a third – relating to properties which are owned outright – has yet to appear. We have called for a joined-up approach to the entire housing stock, to ensure that each sector – owned outright, mortgaged and rented – is treated equally and fairly.

3.7 We have also noted that while much emphasis (and reliance) is being put on the effectiveness of EPCs – there are many properties which have never had an assessment and others which have EPCs which are many years out of date. There will need to be a re-calibration and re-assessment of **all** property, to an equal standard, before property owners can reasonably be obliged to incur improvement costs.

4. The Buy to Let market

4.1 Britain's private rented sector is an essential component of the housing market, providing homes for one in five (20%) UK households. It provides vital accommodation for those who do not qualify for public rented housing and who cannot afford to buy a home of their own.

4.2 The sector has remained vibrant, despite a 'layering' of policy changes introduced over the past decade that have sought to 'redress the balance' between private landlords and first-time buyers. Rather than encouraging an immediate surge in first-time buyers, the initial effect of these measures was damaging to the private rented sector. IMLA's reports *Buy to let under pressure*, published in February 2018, and *Buy to let at a crossroads*, which followed in July 2019, highlighted the impact of these policy changes on private landlords.

4.3 Since then, private landlords have been able to take advantage of the recent Stamp Duty holiday, with Buy to Let purchases increasing to £10.5bn and overall lending (including both re-mortgaging activity and product transfers) reaching £40bn in 2021.[2] However, there could be more unwelcome changes in store for the sector, threatening this growth.

4.4 Proposals from the Office for Tax Simplification (OTS) to reform Capital Gains Tax (CGT) have concerned some landlords as these raise the possibility that CGT rates could be increased to mirror income tax rates. For additional rate taxpayers, this could increase the rate of CGT on residential property from 28% to 45%. The OTS has also proposed reducing the annual CGT exemption from £12,300 to £5,000.

4.5 IMLA has consistently argued that the Government should resist making additional changes that may deter landlords from remaining or further investing in the sector. If significant numbers of landlords exit the market the supply of properties available for rent will fall. While some might argue that this would help redress the balance by making more property available for first-time buyers rather than landlords, a reduction in rental stock will result in higher rent levels – which will make it harder for tenants who want to buy to save up for a deposit. And there will of course always be some tenants for whom ownership is either inappropriate or unrealistic – and they will be hit by higher rents if the supply of properties is significantly impacted.

[2] http://www.imla.org.uk/resources/publications/the-new-%60normal-prospects-for-2021-and-2022.pdf

5. Other market challenges

Finding a solution to the cladding crisis

Funding cladding remediation work on buildings following the tragic Grenfell fire remains a critical issue that the Government and housing sector must find a solution to, and quickly.

The costs of remediation work on existing structures are estimated to be anywhere between £15bn and £50bn. The Secretary of State (Michael Gove)'s announcement (on 10th January) of a proposal to require property developers to come up with £4bn to fund removal of cladding, and new statutory protections for leaseholders, is welcome – but may still leave leaseholders facing large bills for remediation work to address other defects. Legislation must clearly identify where responsibility lies for defective construction and create a fair and proportionate system for funding ongoing maintenance of properties so that leaseholders are better protected in future.

A solution to this hideous issue is desperately needed. Existing funding arrangements are simply not sufficient and need to be put into context – banks collectively paid out in excess of £55bn for PPI claims, and not one of these mis-sold policies caused consequences as deadly as those experienced by the victims of the Grenfell fire.