Safe as houses?

Strengthening the UK's mortgage safety net

Executive summary

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In this Social Market Foundation (SMF) research paper, we explore the topic of "mortgage safety nets" – support for mortgage-holders in the event of loss of income or employment. We consider the economic case for their existence, the UK's policy history in this space and the policy landscape in other countries. We also consider the implications of the Coronavirus crisis for home repossessions, and the extent to which mortgage safety net policy might need to evolve as a result. The report concludes by setting out some principles that should inform future policymaking in this space.

Key findings

Financial resilience among mortgage-holders in the run-up to the pandemic

- **Our analysis of the Wealth and Assets Survey (WAS) suggests that, prior to the Coronavirus pandemic, about 770,000 households were in a financial position that would leave them vulnerable to repossession in the event of a loss of income.** These individuals did not have sufficient financial wealth to cover mortgage payments for a period longer than three months.

770,000
households were in a financial position that would leave them **vulnerable to repossession** in the event of a loss of income

- **Across household income quartiles, the absolute number of such households is greatest in the middle two quartiles, reflecting lower rates of homeownership among those in the bottom quartile.** When just looking at mortgage-holders, the proportion of vulnerable households is much higher among lower income groups – about one in six (16.7% of) mortgage-holders in the lowest income quartile would be unable to pay more than three months of mortgage payments using their financial wealth.

- **By age group, the greatest number of vulnerable mortgage-holders is among those where the reference person[i] is aged 35-44 and 45-54.** Collectively, these two groups account for about 61% of all households that would struggle to pay their mortgage for more than three months in the event of a significant shock to their income.

- **The North West of England had the greatest number of households vulnerable to repossession (102,387) followed by the South East of England (102,104).** The North East of England had the greatest *percentage* of all households (5.1%) and mortgage-holding households (15.2%) that were vulnerable to repossession on our definition.

[i] The concept of a Household Reference Person (HRP) was introduced in the 2001 Census (in common with other government surveys in 2001/2) to replace the traditional concept of the 'head of the household'. In a couple family, the FRP is chosen from the two people in the couple on the basis of their economic activity (in the priority order: full-time job, part-time job, unemployed, retired, other). If both people have the same economic activity, the FRP is identified as the elder of the two or, if they are the same age, the first member of the couple on the survey form.

- **Almost the entirety of mortgage-holders vulnerable to repossession (92%) in 2016-18 were households where the reference person was either an employee or self-employed.**

- **Our analysis of the WAS showed that households where the reference person was employed in retail or manufacturing accounted for a large share of all households vulnerable to repossession** – about a quarter (26%) of the 770,000 vulnerable households we estimate to be vulnerable. With the latest labour market data showing these groups also seeing some of the greatest increases in unemployment, this gives reason to believe that the pandemic could push a significant number of mortgage-holding households into financial difficulty.

Financial resilience among mortgage-holders during the pandemic

- In a February 2021 Opinium survey of 2,000 mortgage-holders commissioned as part of this research, **three in ten (30%) said that their household savings had increased since the Coronavirus pandemic, with a similar proportion (29%) reporting a decrease**.

29%

of mortgage-holders reported **decreased** savings during the pandemic.

- **Mortgage-holding households on lower incomes were more likely to report declining savings since the pandemic – close to half (46%) of those with household incomes of up to £20,000 said that their savings had declined, with just one in ten (11%) in this group reporting increased savings.** Lower earners were also more likely to report that their incomes had declined since the pandemic, further suggesting that Coronavirus has increased the number of financially vulnerable households.

- **Some 14% or mortgage holders in February 2021 said they lacked the savings to cover even one mortgage payment**. Three in ten (30%) could pay their mortgage for no more than two months.

3 in 10 mortgage holders reported they could not pay their mortgage for more than two months

- **These figures are notably higher than those suggested by our analysis of the (pre-pandemic) Wealth and Assets Survey.** In part, this is likely to reflect the negative impact of the pandemic on financial resilience among some groups. It is also likely to reflect households taking into account other costs, beyond mortgages, when answering the survey question. Given other ongoing expenses, such as food and energy bills, the ability to make mortgage payments from savings is further undermined.

- **Across the whole survey sample, the average amount of time that individuals felt they could cover mortgage payments from household savings was six months.** Younger individuals and those in lower income households reported lower average times. On a regional basis, London reported the highest average duration (6.6 months), while the West Midlands (5.1 months) and Wales (5.3 months) reported the lowest.

46%

of households with incomes up to £20,000 reported declining savings since the start of the pandemic.

The UK's mortgage safety net

- **The UK's government-backed mortgage safety net has been eroded in recent years,** leaving a number of households potentially vulnerable in the event of an economic downturn.

- **Support for Mortgage Interest (SMI) has shifted from a grant to a loan that is expected to be repaid, plus interest.** This is despite survey evidence suggesting that this move will cause financial distress for some households. DWP-commissioned polling from Ipsos MORI found that generally, respondents believed the perceived effect of the SMI loan would be negative – over one in three existing SMI claimants (38%) expected it would make their mortgage interest less affordable.[1]

- **Once Universal Credit is fully rolled out by 2024, tax credits will cease and SMI will only be available to claimants entirely out of work.** This could be detrimental to households suffering pay cuts but not outright job losses during the current Coronavirus-induced economic downturn.

Mortgage safety nets in other countries

- On the whole, **it is difficult to find an example of a country with a fully coherent mortgage safety net policy** and, with the available evidence, it is difficult to argue that one country is setting the "gold standard" that others should follow.

- We note, however, **there are a diverse range of approaches to mortgage safety nets, which may provide lessons for developing policy in the UK**. This includes:
  - **Australia allowing early access to pension wealth in the event of severe financial hardship.** To do this, a person must be in receipt of benefits payments from the state for at least 26 weeks consecutive weeks, and that they are unable to pay for "reasonable and immediate" family living expenses.
  - **Hungary setting up a National Asset Management Company (NAMC)**, providing an avenue for debtors to sell their homes and take on a renting option instead.
  - **The US Hardest Hit Fund,** which introduced direct subsidies to help aid mortgage payments and transitions to alternative tenure.

Considerations for policymakers

With these issues in mind, we think there are a number of useful avenues that could be explored for refining the UK's mortgage safety net.

Refining the UK's mortgage safety net

1. **Enhancing "private safety nets"**
2. **Bolstering "social" safety nets through replacing SMI loans with a time-limited grant**
3. **Introducing an enhanced Assisted Voluntary Sale (AVS) process**
4. **Introducing more flexible tenure options**

1. **Enhancing "private" safety nets** through:

   A) **Encouraging wider (but not mandatory) uptake of mortgage payment protection insurance.** We are reluctant to suggest that the right approach here would be a mandatory insurance scheme, not least because of legacy of insurance misselling in past years which has impacted the reputation of such products. However, bought and sold correctly, and with a price-competitive market for products, such insurance could play a key role in preventing repossessions.

   B) **Adopting the approach of Australia, and allowing individuals to draw on pension wealth in a case of extreme financial distress.** The ability to do this should, in our view, be subject to strict criteria – given the risk of pensions becoming perceived as emergency savings, and the risk of replacing a "home repossession problem" with a "lack of pension income problem" in older age. Nevertheless, for some segments of the population, drawing down pension wealth might be an appropriate last resort option.

2. **Bolstering "social" safety nets through** r**eplacing SMI loans with a time-limited grant,** as recently proposed by the Centre for Policy Studies sponsored by the Joseph Rowntree Foundation. This would ensure that those suffering a temporary loss of income receive support for housing costs during a period of hardship, without the risk of building up further financial issues from having to take on an additional loan.

   Beyond a period of grant payments, treating SMI as a loan and making the benefit time-limited may be justified. This is not just because of costs to the state but, where individuals are likely to be suffering a permanent or long-lasting loss of income, the best option may be to encourage them to consider a change of home or change of tenure within the same home.

   The waiting period for receiving SMI should also be reduced to 13 weeks. Our analysis has identified a significant number of households with limited financial resilience, for whom the current waiting period of 39 weeks could lead to significant financial distress.

3. **Introducing an enhanced Assisted Voluntary Sale (AVS) process, which could include:**

   A) Removal of early repayment charges (if applicable) to help sell a property before the mortgage term ends.

   B) Cash payments towards rent or deposit on new rental property.

   C) Providing cash payments to help homeowners to make necessary improvements to their home to help a sale

   D) Where equity in the property is available, lenders could provide a cash advance of this equity to help the household

   E) Assistance with estate agent fees on sale of their property

   F) Government taking a second charge on the property, which could be advanced to the homeowner to help towards rehoming them. When the lender sells the property, the money is repaid to the government, and any leftover goes back to the borrower

4. **Introducing more flexible tenure options.** Some households would benefit from a new form of tenure in which a freehold is held by a new trust entity, with trustees being the lender and the householder. In contrast to shared ownership, individuals could increase or decrease their ownership stake by incremental amounts rather than large equity shares (e.g. 25% steps).

   Such an approach would make it easier for individuals to find a balance of mortgage and rent payments that works for them. It might also be useful in circumstances where the property market is particularly illiquid, with lengthy average times to sell a home. Individuals could rapidly shift tenure by selling to their lender.