Where do we go from here?
How UK mortgage lenders see the UK mortgage market - past, present, and future

December 2012
Director General's foreword

This report is a self-evaluation of the mortgage industry by its leading members - the mortgage lenders who provide the lending that enables the UK housing market to transact. It will give you an insight into what our members think about their market, where it has come from and where it is going. It sets out their views on how its resilience, sustainability, and flexibility could be improved for the benefit of its customers.

It is written now because the industry has been going through a long and significant period of retrenchment, in the aftermath of the financial crisis. The market has contracted but in some important respects is now healthier than it was. This report captures how past mistakes can be avoided in the future and how past successes – of which there are many – can be consolidated.

Above all, it suggests how the UK mortgage market can best go on delivering its principal function; for well over 160 years, UK mortgage lenders have been helping ordinary people to buy homes in which to live (even since the credit crunch it has helped 1 million first-time buyers to enter the housing market). We want this to continue and have set out some ideas of how it can.

This is unashamedly a report on the mortgage industry from the mortgage industry. This is not because we discount the importance of others’ views. We appreciate the perspectives of Government, regulators, builders and other businesses in the housing and mortgage markets, consumers themselves. We hope they will find this report useful as a catalyst against which to calibrate and share with us their own views of how they think the mortgage market should develop in the future.

In compiling this report we found great consistency in the overall themes from all the lenders to whom we spoke. But consistency of theme does not imply an industry-wide consensus on every point and we do not pretend that there is unanimity where it does not exist.

Paul Smee
CML director general
December 2012
Introduction

This paper is both an audit of what has happened in the mortgage market and what needs to happen to create the healthy mortgage market of the future.

It aims to capture what has gone right as well as what has gone wrong in recent years, so that we learn from the recent past and have a multi-dimensional view of it.

It also looks to the future, conscious that, for well over 150 years, UK mortgage lenders have been at the very heart of providing the means for a huge swathe of the UK’s population to be housed decently, self-sufficiently, and economically and clear that the sector intends to continue to play that role well into the future.

This report shows how we can achieve this.

It is based on views expressed during structured interviews with the members of the CML’s Executive Committee (main board), as well as subsidiary questionnaires involving other CML members. We wanted members to be frank in their views, so we conducted the interviews on a confidential and non-attributable basis. As the CML represents 95% of mortgage lending, this approach has provided a comprehensive snap-shot of how market participants feel they got here; where they feel they are going; and what they think needs to happen to make a better mortgage market for everyone.

We undertook our structured interviews with CML board members during the summer. Most of the interviews lasted between an hour and an hour and a half. Unsurprisingly, we recorded a variety of views, not all of which we can capture in the space of a short report. While we make every effort to provide a fair and balanced summary, we apologise for any errors or omissions.

We hope the results will act as a helpful contribution to debate both within the mortgage industry and beyond it, among regulators, commentators, consumer representatives and the media.

We would welcome your feedback. Please email nat.mlinar@cml.org.uk if you have any comments.
The current environment

Although this is not the place for a detailed history, a bit of background is helpful -

- The mortgage industry is hugely important to both housing and the economy in the UK. Despite the problems of the past few years, mortgage lenders are still overall providers of solutions, far more than problems, as far as the UK is concerned. They are currently lending on around 1 in 3 UK homes, and more than 1 in 3 home-owners had a mortgage in the past that they have now repaid. In addition, UK lenders hold around £164 billion of lending to private landlords, and £42 billion of lending to social landlords, involving perhaps another 4 million homes being partly financed by their lending. Mortgage lenders are employers, corporate taxpayers, and providers of a service that has been valued by consumers and central to helping them to fulfil the strongly embedded UK aspiration for home-ownership for well over 150 years.

- Mortgage lending has not generally been a high risk activity – for lenders or borrowers. The vast bulk of existing mortgage loans, even those which would not today be advanced under current lending standards, are performing. It has sometimes been difficult to get the message across that, while risky US mortgage lending was ultimately responsible for the collapse in confidence that closed global funding markets, it was this collapse in funding that wreaked such havoc on the UK financial system rather than the underlying quality of the aggregate UK mortgage lending balance sheet. However, trust in mortgage lenders has quite clearly been damaged, and continues to be damaged, by wider banking issues; and the crash did expose some racier business models.

"The financial crisis didn't show us that retail funding was good and wholesale bad. What it really showed us is that you need a mix of funding in case one element of it suffers a shock that can affect the whole financial system."

- Banking and the wider financial system in the UK are going through huge change, in terms of both regulation and culture. The mortgage market specifically is deeply affected by regulatory change at a structural level (through prudential regulation and capital requirements, and the current debate about macro-prudential tools such as loan-to-income or loan-to-value caps), and also through conduct of business requirements (where the FSA’s Mortgage Market Review - soon to be inherited by the emergent FCA - is introducing wholesale changes). As well as these direct changes, indirect impacts are emerging driven by change in other areas of financial services, including the Retail Distribution Review, which does not directly affect mortgages but may create a ripple effect within the mortgage market.

- It is actually very difficult to assimilate and interpret what the aggregate effect of all these changes, which are themselves works in progress, will add up to for the UK mortgage customer. But one effect already apparent is the "lend less/lend more" paradox. The direction of regulatory travel leads inexorably towards mortgage lenders adopting a highly risk-averse stance - driven both by capital and conduct considerations. So they should lend less. Yet social and economic policy quite clearly points towards a different objective - of lending more liberally to support housing construction, increasing supply and so creating spin-off demand for associated services - thus creating jobs, and growth in the wider economy. So they should lend more.
Where we've come from

Understanding our history can help us understand where we are now. A hundred years ago, about 90% of all homes were privately rented and 10% owner-occupied. By 1938, as a result of the inter-war objectives of increasing the volume and quality of the housing stock, owner-occupation had risen to 32%, with 10% rented from the public sector and 58% privately rented. Owner-occupation became a stated policy goal and measures to promote it over the following half century included, perhaps most famously, the Thatcher era’s Right to Buy.

Throughout this period, the major providers of housing finance for owner-occupiers were building societies. But by the late-1980s, financial services deregulation and rising competition had resulted in a transformation in the mortgage market. Not only had banks begun to compete for mortgage business, but a new breed of "centralised" mortgage lenders had emerged, without branches and funded through wholesale sources rather than retail savings.

Against this backdrop of increased competition, and with a Building Societies Act in 1986 that, among other things, allowed building societies both to diversify and to demutualise, Abbey National became the first building society to become a bank in 1989. Through the 1990s, further demutualisations and acquisitions included Cheltenham & Gloucester, National & Provincial, Alliance & Leicester, Bristol & West, Halifax, Northern Rock, Woolwich, Birmingham Midshires, and Bradford & Bingley.

In 1986 the building society sector accounted for 72% of gross lending, with banks accounting for 24%, and other financial institutions the remaining 4%. By 2000 banks accounted for 70% of gross lending, with building societies accounting for 21% and other financial institutions 9%. In 2007 - just before the financial crisis - banks accounted for 68% of gross mortgage lending, building societies for 14%, and other financial institutions for 17% (having overtaken building societies in terms of ending volume for the first time the previous year).

By the mid-2000s, the combined effects of a highly competitive and liberal financial services landscape, strong demographic growth, and limited new housing supply, meant that house prices had risen significantly above the previous historical relationship to earnings, creating something of a Catch-22 for both borrowers and lenders.

![Chart 1: UK House price-earnings ratio](source: ONS and CML estimates)
For many borrowers, getting onto the housing ladder involved borrowing at relatively high loan-to-income and loan-to-value ratios. But failing to borrow meant running the risk of permanent exclusion from the market. Homeownership peaked at around 70% in the early years of the new Millennium, with over 80% of adults - then, as now - prizing home-ownership above other forms of housing tenure, and wanting to achieve it for themselves.

For many lenders, lending up the risk curve could to a large degree be offset by an increased understanding of predicted borrower behaviour (based on credit bureau data, which provided a richness of understanding not available to previous generations of lenders). It was now also possible to offset risk to stretched borrowers by offering them fixed rates (which, although common until the 1950s, had fallen into disuse in the UK mortgage market, being almost entirely replaced by variable rates that could change as frequently as monthly).

Overall, the risks looked manageable - and, indeed, the performance of mortgages through the downturn largely bears this view out, even if the pricing of such loans now looks to have been less risk-based than it might have been, driven by hefty competition among lenders.

On the other hand, for lenders, failing to lend in line with the market meant short-term business risk. Failing to match the product offerings of competitors meant losing market share. And losing market share meant failing to match the growth and profitability of competitors - particularly as pricing became ever more competitive and margin ever thinner. Volume was the way for lenders to deliver successful balance sheet results.

"I am familiar with a lending business that saw an average lending margin of around 55 basis points in the 1990s, but by 2006 it was less than 20 basis points - which meant it had to do three times as much business just to stand still in terms of return".

But while lenders understood that they were moving up the risk curve in terms of their lending, and some would even acknowledge that this was not rational, based as it was on the perceived need to compete, more than on the fundamental metrics of lending, none foresaw (and neither did the regulators) the systemic collapse in wholesale funding markets that subsequently caused our financial sector problems and resulted in the draconian pendulum swing back to lending constraints. The point of this history lesson is simply to describe how far - and how fast - the landscape in terms of mortgages can change. Change in the mortgage market has been a permanent feature of the last three decades. Yet anticipating the form it will take is difficult.

Throughout this period, and right up to the present, regulation forms a pretty much constantly changing background scene. First, the deregulation of financial markets that saw banks - and then specialist lenders - enter the mortgage market. Then, the advent of self-regulation in the mortgage market through the CML's Mortgage Code - and an independent monitoring and enforcement body in the shape of the Mortgage Code Compliance Board - that paved the way for statutory FSA regulation of mortgages to home-owners in 2004. Since then, the major changes to capital and liquidity requirements, the dismantling of the FCA into the forthcoming twin peaks of the Prudential Regulatory Authority and the Financial Conduct Authority - and the emergence of a new Financial Policy Committee which may or may not end up using macro-prudential tools such as loan-to-income or loan-to-value caps - have begun to change the post-financial crisis landscape significantly. For mortgage lenders, all of this is running in parallel with significant changes coming around the corner as a result of the Mortgage Market Review and its widespread changes to the mortgage conduct of business rules. And to top it all a new European Directive is also about to be finalised, which may or may not be consistent with the changes announced by the FSA.

But if neither market forces nor regulation are the answer to creating a sustainable, rational market that works well both for lenders and for consumers, what is? This is where lenders' views come in, as this is what we asked our members about. The rest of this report captures a flavour of what they said.
What was good about the immediate pre-crunch mortgage market?

It’s tempting to demonise the pre-crisis mortgage market, and many have done so. But it would be a mistake to ignore its positive features. So we asked lenders whether there were aspects of the pre-crunch market that had been better for consumers than the market is now.

This was probably the main area within the whole survey on which there was the greatest consensus. In essence, lenders identified three main features of the market which were - at least partly - better for consumers pre-2008:

- **Choice**

  Virtually all respondents cited the choice of mortgages available to consumers as a positive feature of the mortgage market of the past. That choice covered not only various different interest rate options, but also a choice of repayment method by using the interest-only mortgage product and combining it with a personal choice of repayment strategy. It also included greater levels of choice for people who are responsible and good credit risks but do not meet lenders’ standard criteria (by virtue of having fluctuating and less predictable incomes, or complicated circumstances such as recent self-employment).

  At the same time, most respondents also said that the high level of choice available was only positive if used responsibly. Some expressed concern that it had previously been possible to "game" the choices available, rather than using them for their intended purposes or intended target customer groups. Examples included customers self-certifying income when normal income verification would have been possible, and most respondents said that such activity had made it inevitable that the FSA would now require income verification in all cases. While they welcomed the clampdown in inappropriate practices, they also reflected that one consequence was that some borrowers who would have used self-certification entirely appropriately would now no longer have that choice available to them.

  "I think it says something, at least about the mainstream mortgage market, that most of the mortgages that were lent at the height of the boom are still performing well."

- **Pricing**

  Most respondents said that the highly competitive nature of the mortgage market prior to the financial crisis was a significant benefit to borrowers of the time - although they also observed that some of the pricing was neither rational nor sustainable for lenders themselves, and hence not a genuinely positive feature of the market overall.

  Many respondents pointed to products such as sub-base rate trackers, or loss-leading two year fixed rates offered at prices lower than the actual cost to the lender, as examples of pricing that worked to the benefit of the particular consumers who chose them but were not rational for lenders, nor beneficial to the post-crisis generation of borrowers. For today’s customers, mortgage pricing is influenced not only by the current costs of funding, capital and distribution, but also by the fact that some lenders are needing to restore balance sheet strength through new business to make up for weaknesses that arose through the pricing of previous business.

  Many lenders expressed concern that, in a market in which there was so much choice, so many borrowers appeared to choose a 2-year fixed rate mortgage as the most appropriate for their needs. Some expressed doubt about the advice process, finding it implausible that a 2-year fix could conceivably be the best choice for such a high proportion of borrowers. Others said it showed that the aggressive competitive pricing around that particular product type distorted the other considerations that ought to be relevant factors in deciding which mortgage to choose.

  Most lenders expressed an expectation that pricing in the future would be more risk-based, and more sustainable. Most saw capital requirements as a significant influencing factor both on price and on the mix of business that lenders would undertake in the future. On
balance, virtually all respondents saw this as a better approach than the past - yet recognised that from the consumer perspective, the pricing benefits that existed for a period of time in the heady pre-crunch environment are unlikely to return.

**Access to mortgages**

The third element of the market that lenders thought was previously good for consumers was the relative ease with which they were able to access mortgage finance (and hence the housing market). More than choice and pricing, access to the market is the area where lenders perceive today's borrowers as being at a significant disadvantage compared with the past (although it does need to be borne in mind that access to the market had already become more difficult due to rising house prices before the financial crisis, and that the level of owner-occupation had already begun to decline).

Reduced access is manifested both in a greater price differential between borrowers who have substantial equity and those who have only a modest deposit, and also in greater difficulty in fulfilling lender requirements in terms of credit status, income verification, and other credit risk assessment factors. Lenders acknowledge that today's conservative conditions, while likely to result in less risk to both borrowers and lenders, significantly reduce the ability of some consumers to access the market. Lenders are split between seeing reduced access and conservative lending requirements as a permanent corollary to a culture and regulatory system in which the principle of caveat emptor has been eroded, and a temporary response to funding and capital market conditions that will ease if and when wider market conditions do. The extent to which lending criteria are tightened or loosened is one important influence on whether access to homeownership, for those who desire it, is achievable.

**What wasn't so good about the pre-crunch market?**

In many ways, those aspects of the market that with hindsight are seen as poor for consumers are very closely aligned with those that were seen as good. Two sides of the same coin can produce very different outcomes, depending on exactly which consumers we are talking about.

The positive qualities of ease of access, highly competitive pricing, and large amounts of consumer choice (both of mortgage products themselves, and of how to buy and use them) become negative and risky when used irresponsibly and to excess. Through this lens, lenders identified how a number of features of the "boom" market became distorted and with negative consequences for consumers:

- **The illusion of permanent house price inflation**

  Lenders and borrowers experienced an extended period of high house price rises. This created a source of wealth and a sense of financial wellbeing for many borrowers, who became used to entering the market and immediately seeing their equity (and hence their notional wealth) grow. Rising house prices also provided an increased equity cushion as a risk buffer for lenders, who saw their loan-to-value ratios on their existing loan portfolio diminish almost as soon as they granted a loan.

  But house price inflation also resulted in a significant shift both in affordability and risk dynamics (a 90% mortgage on a house worth, say, three times its owners’ income is not the same as a 90% mortgage on a house worth seven times their income). Equally importantly, it affected attitudes. The perceived importance of the borrower's "personal covenant" - that is, their promise to repay the loan irrespective of the value of the house - was eroded because it seemed irrelevant.

- **An increase in lending (and borrowing) risk**

  While most lending actually remained fairly conservative even through the boom years, the illusion of permanent house price inflation gave rise to a relaxation of some other risk assessments by
some lenders in particular parts of the market. While "self-cert" lending is probably the example that sits highest in public consciousness, other more subtle examples included a higher reliance on automated systems (on property valuations, for example), that in a less buoyant environment of house price inflation might have been used more conservatively.

In practice, this has not resulted in widespread problems for mainstream lenders or borrowers. But it has resulted in pockets of difficulty in sub-prime parts of the market, and we do not underestimate the effect of such difficulties on individual households concerned. It is also notable that those lenders which relaxed their credit risk assessment and processes the furthest are, generally speaking, those that are no longer in existence (although this is at least as much to do with their funding mechanisms as with the performance of their underlying lending).

- Increased complexity and a higher risk of confusion

For consumers, choice can be a double-edged sword.

On the one hand, choice and variation makes it more likely that a suitable product can be found to meet the customer’s particular needs.

On the other hand, there is a higher degree of expertise and effort involved in finding the needle of a suitable product in a haystack of many, many others.

In essence, mortgages are relatively simple financial products. But most lenders feel that the pre-crisis market - and, to a significant degree, even the market of today - has fed a culture of ever-increasing complexity that does not always serve consumers well. It has also meant that "advice" is now more commonly perceived as a need for mortgage customers than would be necessary in a simpler market with fewer choices.

- The unintended consequences of consumer protection

In parallel with the rise of increased complexity, there was a simultaneous rise in the level of consumer protection offered through regulation. This, too, is a double-edged sword in the view of lenders.

On the one hand, appropriate levels of consumer protection are clearly both necessary and desirable, especially on a product as important as a home-owner’s mortgage.

And lenders would acknowledge that there is an “information asymmetry” between customers and lenders, with customers at a disadvantage as a result.

On the other hand, there is a risk that the principle of caveat emptor - let the buyer beware - becomes entirely eroded and morphs into a "someone is to blame" culture, in which consumers become unwilling to make the effort to research and understand financial products, or to take responsibility for their choices, if those choices subsequently turn out less well than they expected.

Many lenders are alarmed at how little awareness or interest consumers show in their own financial affairs. Both industry and regulators have, over long periods, grappled with attempts to increase financial capability but seem rarely to engage with those consumers who most need better skills to appreciate what is available.

This disengagement leads to a significant number of consumers making the assumption that if lending is available, then it must be safe/right for them (fed by the perception that they do not need to educate themselves, because regulation will protect them).

This can leave consumers potentially vulnerable to scams and unscrupulous sales tactics, as well as genuine confusion about making good choices for their own circumstances.

It has led many lenders to feel that such customers would be better served by a simpler set of mortgage products. The simplicity versus choice dilemma is one of the thorniest issues that our survey identified. We return to it later.
"I don't regret the loss of 100% mortgages. Above around 95% the customer behaves as if they have no "skin in the game".

"Warning signs should have been spotted by government, regulators, lenders and consumers."

- A distraction into a focus on business relationships rather than consumer relationships

Many lenders felt that the highly competitive nature of the mortgage market - and the drive for market share - in the pre-crisis period skewed the focus of lenders' attention too far onto their business relationships, at the expense of a clear focus on customers themselves. Many lenders felt that the industry had in the past effectively been designing some mortgage products primarily for distributors as though they were the client, rather than unequivocally for borrowers as the real client.

At the time, lenders felt that this was because brokers were close to consumers and had a clear understanding of their needs. With hindsight, some lenders think they allowed brokers to have too much influence on product design. Given the obvious incentive for someone who gets paid a one-off fee for selling a product to ensure they have repeat sales opportunities as often as possible, a number of lenders are suspicious about whether the high prevalence of 2-year product sales invariably matched consumer needs.

Lenders collectively accept that they allowed themselves to be drawn into generalised assumptions over prevailing market norms, rather than exercising objective judgment.

Business success was determined by growth and market share, since these were the perceived drivers of value within the business. But growth and increased market share could only be obtained by ever more competitive pricing, leading to mainstream business being written on increasingly narrow (sometimes negative) margins, and profitability being delivered primarily through higher volume and/or higher risk lending, and a relatively inert "back book".

"To not grow - or to shrink - would have been seen as failure."

"It was a volume driven market - Boards were always looking for more."

"It was difficult not to do what the rest of the market was doing - business models exacerbated the drive to do new business."

"There was a high level of cross-subsidy between the front book and the back book."

(ironically, some of those borrowers who benefited from the very cheap new business pricing may well now also be the same borrowers benefiting from low SVRs)
"Although I really dislike absolute bans on particular lending practices, the actions of any individual lender can end up reflecting on all lenders. So I think one thing that was wrong was that we didn’t challenge what looked like bad lending simply because the FSA wasn’t intervening to stop it."

"Intermediaries (and particularly packagers) fanned the flames, but lenders made the playing field and set the rules of the game. Lenders relied too much on FSA authorisation of intermediaries."

So much for the past, what about the future?

As far as the lending landscape is concerned, the past is another country. If the pre-crunch market sought growth at the expense of controlling risk, recent market conditions can reasonably be accused of seeking to control risk at the expense of growth.

Many lenders think that both market conditions and the regulatory pendulum have swung too far, yet see this as inevitable as a response after the financial crisis. Most lenders expect conditions to ease over time, but few lenders expect this to be anything other than a very gradual process.

Most lenders do not regard current market conditions as "normal", and even identifying what a normal market looks like is difficult. So instead, we asked lenders to tell us what they thought a good market looks like, for both lenders and borrowers.

Lenders did not hold identikit views on this question. At the extremes, some persuasively argued the case for a "good" market being characterised by minimal distortion and intervention, with regulation based primarily on transparency, where lenders and consumers transact at levels and on terms dictated by competition. Others equally compellingly argued that a "good" market is one that offers high levels of consumer protection, recognising the relative imbalance between the knowledge and power of consumers and lenders, with substantial regulation that protects both consumers and lenders from themselves (and each other).

Most were somewhere in the middle. But they tended to agree on a number of common characteristics.

What does a "good" mortgage market look like?

Our respondents had a very wide range of views on what a good market looks like. Broadly, these clustered into the following characteristics:

- **It works within a good overall housing market**

  Lenders felt very strongly that a good mortgage market can only truly exist within a good overall housing market, however effectively lenders run their businesses. A good housing market is essentially one in which there is a reasonably good balance between supply and demand, where there is sufficient funding and finance available to provide the necessary liquidity within the home-ownership sector, the private rented sector, and the social housing sector, and where tenure choice is therefore not artificially distorted by dysfunctional elements of the market, or by particular incentives or disincentives that mean there is no genuine choice for households.

  Lenders accept that they need to be receptive to providing "housing finance", not just "mortgages". This includes commercial lending to developers, housing associations, buy-to-let and large-scale private landlords. But they feel that housing policy - the levers through which housing supply is managed, as well as the mechanisms that help to create an environment in which different tenures can complement each other to the benefit of households with different housing needs - is something with which they engage, but not something that they control; they feel that there is a lack of clarity around the government's long-term vision for housing supply in the round.

  If finance is readily available for all types of housing, tenure becomes a matter of genuine choice, rather than a reaction to the lack of it. Lenders would see this as a positive characteristic of a healthy housing market.

- **It provides access**

  Lenders think that the mortgage market should be accessible to
Credit-worthy borrowers of all types. Conditions in the funding markets, regulatory arena, and competitive landscape are all relevant in determining whether the objective can be met.

Lenders see a market that is providing access as one where the variety of lending available and taking place is a good fit with consumer requirements. So that means that there should be a good spread of loans available, from a wide variety of lenders, for first-time buyers, home-movers, those seeking to change their mortgage, self-builders, and those seeking intermediate tenure options, such as shared ownership or shared equity purchases supported by a mortgage.

Lenders generally think access is most likely to be achieved if the market contains a variety of different types and sizes of lenders, and not too much business concentration within the hands of a very few. From an objective standpoint, rather than the interests that may serve an individual existing lender, lenders believe that a good mortgage market is likely to be one which is receptive and open to new lenders.

"Although new lenders aren’t a silver bullet, a good market would see less concentration of business among so few large lenders."

- **It is flexible**

A number of lenders said that they felt a good mortgage market should respond to the fact that we live in a world where change is normal. A good market should recognise that consumers’ plans may alter over time, their circumstances may change unexpectedly, their housing needs may evolve, and their trade off between risk and reward would also vary at different times.

Over-paying, under-paying, flexible tenure and moves between tenure were all cited as examples of flexibility that can be good for consumers and that a good mortgage market should be able to cope with.

Lenders see a good market as one that is capable of innovating pre-emptively for foreseeable changes.

"A good market would reduce the frictions that can make it difficult to move".

- **It offers value**

Most lenders defined a good market as one that offers long-term, sustainable value for both borrowers and lenders. Products and relationships should be predicated on aspirations that they are long-term (rather than just short-term until the end of any "teaser" period), on pricing that is realistic (rather than loss-leading and dependent on future customer inertia), and on design that actively tries to ensure that shocks that could knock value off course are minimised where they can be. Many lenders felt that a good market:

  - has enough competition to give consumers a good deal, but not so much that it dilutes proper credit risk assessment, or creates an environment where lenders price their products irrationally
  - prices for risk against a competitive backdrop, resulting in reasonable profitability but also reasonable consumer pricing.

- **It is safe but not risk-free**

Lenders see a good market as one that is safe in so far as it values sustainability, rational behaviour, and the avoidance of shocks that could reasonably have been anticipated (by lenders or borrowers). However, borrowing or lending carries intrinsic risk for both parties, and cannot be made risk-free. But a good market values risk mitigation where it is possible and can be achieved at reasonable cost. Some of the things that lenders said they thought were characteristics of risk in a good market included:

  - It is not risk-free for either lender or borrower, but risks are assessed, controlled, understood and (where possible) mitigated
  - Mortgage arrears and repossessions only occur as a result of unpredictable changes in circumstance, not as a result of the loan itself
It doesn't create distortions through the distribution/sales process.

It is transparent and products are understandable to consumers.

Regulation balances and reduces pernicious effects (on consumers and the financial system) that recent history shows can arise when market forces are unfettered.

It's funded through a mix of sources, not just one.

It can ride economic and housing market cycles and can smooth the peaks and troughs of boom and bust.

Doubtful practices by outliers are dealt with promptly and pre-emptively by regulators.

But regulation is a minimum standard, not a maximum - the fact that something is "compliant" should not be the only yardstick of whether it is good business.

It evaluates risk on its merits, not because of concerns that regulators (or other third parties) have on a particular risk.

"Funding is key. There needs to be a balanced market, with access to wholesale markets."

"A good market ought to be able to cope with some higher risk lending. But if one element is risky - say a high loan-to-value - then all other elements should be strong. But we ought to have a market that allows near-prime lending, and we ought to have a market that can take a calculated risk and lend to a young customer with good prospects. It's not right to try to return to a 1950s throwback."

What are the influences that can act against achieving a good market?

In theory, all the elements of a good market should be good both for the customer and for the lender. But, in practice, tensions create imbalances which are rarely acknowledged or articulated.

Some examples are:

- **Short-termism**
  Many lenders reflected on the detriment to the market that they felt arose from both businesses and consumers taking a short-term view, even though there was a long-term contract between them.

  Many respondents felt that in the boom years, lenders, brokers, and borrowers were all unduly influenced by prevailing conditions, rather than by the possibility that, in the future, these might change. There was consequently a fixation on growth and market share, which delivered profitability in the short term but was not based on a sustainable long-term business model. Products were designed and sold with a focus on short-term performance rather than long-term value.

  In the case of borrowers, short-termism can result in a disproportionate focus on initial costs rather than long-term value and product features. This can lead to consumers choosing mortgages whose characteristics are not a good long-term fit with their needs.

- **Opportunism**
  Human nature dictates that opportunism will be at play from time to time, and this may be on the part of consumers, brokers, or lenders.

  "There are times when it feels as if consumers can be wilfully naïve. If someone gives them a way to borrow, they'll take it, whether it's good for them or not."

- **Complexity**
  Complexity within a product is not invariably bad. It can lead to a design which meets needs that...
a simpler solution would not adequately address. But it can also have unintended consequences, especially if the product ends up with a consumer who is not able to evaluate the consequences of complexity. (An example: a bargain-basement mortgage rate may be seen as a desirable product feature, in an environment where this feature is seen by consumers as the most important consideration when choosing a mortgage. Yet to achieve it, on a sustainable basis for the lender, may mean that it is accompanied by a complicated array of other fees and charges). Complexity can be introduced, for reasons which are more to do with market positioning than consumer interest.

"Products still lack clarity today. Anything that can be done to simplify KFIs would be good. It's difficult for customers to see the wood for the trees."

"Consumers look at products, not risks".

So, lenders think that the long-term interests of lender and borrower are (or should be) well-aligned. But there are pressures in practice which can cause them to diverge. Lenders see an important function of regulation as the counterbalance to this divergence.

"There is a natural tension - the consumer wants the lowest possible price, the lender wants a decent return. In the pre-2007 market, lots of lenders squabbling for the same business meant consumers won in the short term."

"It's difficult to determine where the tipping point is between too many products and too much risk."

Do we currently have a good mortgage market?

This was probably the question that elicited the most divergent views from lenders.

Many lenders felt that the current market had become too conservative and risk-averse; this was down to two factors:

- regulatory over-reaction to the lessons of the financial crisis,
- lenders’ own collective re-focusing on de-risking as the dominant feature of business plans for the foreseeable future.

These lenders commented that most mortgage borrowers had continued to pay their mortgages throughout the downturn; that aspirations to home-ownership remain extremely high; that a good market should be characterised by choice; that borrower risk appetite should be dictated by personal preference rather than external control; and by concern that, in any case, a highly risk-averse first-charge mortgage market would likely mean that consumers who wanted to borrow would still find a way to do so outside the regulatory perimeter, without the benefits of robust consumer protection.

On the whole, these lenders felt that capital prudential controls - which have already been strengthened and are set to be further strengthened still - were the most effective form of regulation to influence the behaviour of the market.

But there were other lenders who felt that the current market had returned to firm lending fundamentals, and that overall the conduct-of-business changes under way to be welcomed. These lenders tended to express concern about the tendency for markets to gravitate under prevailing market conditions towards similar processes and practices that were difficult for individual businesses to resist even if they seemed irrational. These lenders would also accept that current conditions were causing difficulty for first time buyers and mortgage prisoners.

"The current market is actually pretty good for some current lenders: mainstream business is now far more sensibly priced, and new lending is being written on a far more sustainable basis as far as future profitability is concerned. That's not the same as saying it's a good market overall."

Many lenders recognised both perspectives.

Overall, there were few lenders who felt that the general direction of regulatory travel was wrong, despite reservations about practical implementation.

But there were some concerns about whether it is too difficult for newer or smaller lenders to compete effectively with larger, established incumbents - and whether current conditions reinforced this state of affairs.
And there were concerns about groups of customers who are disadvantaged by change - notably, those who are credit-worthy but whose income is less predictable or whose circumstances are unusual, and those who now find themselves unable to borrow even though they were able to in the past.

"I don't know whether the market specifically needs new entrants or just more activity from inactive current lenders. New entrants face high regulatory hurdles - and there are significant entry costs."

First-time buyers are seen as a special case. Lenders in many cases feel they are on the horns of a dilemma: while increasingly differentiated, risk-based pricing is entirely the right thing to do both in business terms and for the stability of the financial system (and is firmly entrenched through regulatory capital requirements), consumers can see it as having a perverse outcome in that those who can least afford it are charged the highest price and are thus kept out of the market. But the alternative would be equally perverse - if pricing for riskier lending were cheaper, then less risky borrowers would inevitably pay more, for the lender to achieve the same overall rate of return. Neither of these outcomes necessarily feels like "a good market" to lenders.

So many lenders feel inhibited from serving first time buyers and "non-standard" borrowers from a combination of regulatory factors and market factors. There is some concern that well-intentioned regulation, combined with additional self-imposed "buffers" against both prudential and conduct risk, may, as a consequence, permanently exclude some legitimate borrowing, as well as some legitimate lender practices.

"I understand why it has gone, but logically fast-track lending should never have been bundled together in regulatory terms with self-cert. Properly used, with the checks and balances to prevent abuse, there is nothing inherently wrong with fast-track."

If this inhibition continues, one likely outcome could be a contraction in home ownership and lenders are concerned that the repercussions of this are not being addressed by those forming housing strategy as a whole.

Self-help, industry-led initiatives designed to support the market - such as the recently launched NewBuy scheme to offer 90-95% loans backed by a developer-funded indemnity on new-build property - tend to suffer from inflated and unrealistic expectations of how much they will impact the overall market; they cannot form on their own a comprehensive housing strategy. Lenders are willing to back these initiatives and welcome what they contribute, provided that the contribution is not exaggerated.

"It will take a decade to repair problems and get to a good market. Funding remains the major issue."

"The market is moving towards a better position, even if it has had to be pushed. It shouldn't be stifled by excessive regulation."

"We need to reinvigorate competition in high loan-to-value lending. But I think it needs some kind of a collective response. If individual lenders simply duck out of this market it has a very negative impact."

"There is still a significant process of balance sheet repair under way, funding markets are still unreliable, the economy is sluggish, there is a general unwillingness to innovate, and there is a significant disconnect between base rates and the true costs of mortgage funding and operations. So I think there are 5 years of ongoing difficulty ahead. But in the long term I hope we will have a rational market, with a reasonable number of active lenders, transparent to consumers, and where pricing is sustainable and clearly related to the true costs of provision."
How do we get to a good market?

Lenders tended to share common views about what should be done to help the mortgage market develop in a positive way. Lenders think that this good market depends on actions and thought not only by the lending industry and its professional contacts, but also by government, regulators, and consumers themselves.

Taking the long view

The long-term nature of the mortgage market and the commitment to it needs to be recognised, and embedded in how all participants behave. Long-term markets are unlikely to be well-served by short-term strategies. For this reason, many lenders are now redefining their thinking on how they are designing, selling, and administering mortgages. A number believe that the successful business models of the future will reflect a paradigm shift: the focus on new business acquisition will become relatively less important, while the retention of good quality business delivering sustainable returns will become more important. If true, this could have a number of implications. It could affect the dynamics of mortgage distribution, both in terms of how lenders work with brokers, and in terms of how they manage their own direct business channels, perhaps with less focus on sale and more focus on retention.

Putting housing at The Thick Of It

A stable market, in lenders’ view, also needs a coherent alignment of housing market objectives with tax, welfare and social policy objectives. At present lenders feel this level of vision does not exist.

“I’m not sure about government interventions that distort markets. But the macro-economic environment drives everything. We need stability in the economy to plan, but it feels as if it’s a long time off. It would help if we could de-politicise the economic environment.”

Lenders see the following political factors in play:

- Property taxation is a political hot potato; meaningful change appears unaffordable, or unachievable, or both.
- Welfare and social policy tend to consider housing issues purely at a cost level, rather than taking a cost/benefit approach to different alternatives. There is an honourable exception in the local authority mortgage rescue scheme, which gained traction partly by virtue of costing less than the alternative re-housing and housing benefit costs that would otherwise be incurred by local authorities. This has been a success and shows how a holistic vision can work.
- Political attitudes to the private rented sector are schizophrenic, just as buy-to-let has been perceived as a mixed blessing (on the one hand, delivering a viable private rented sector and increasing choice; on the other, competing with home-ownership objectives and keeping house prices higher than they otherwise would be. Government is actively seeking to manage out of the social housing sector those households who could realistically participate in the open market. But intermediate tenure - such as shared ownership and shared equity - is constrained (from national lenders’ perspective) by the highly fragmented nature of its delivery at a local level, making it difficult for many lenders to commit to unequivocally or without disproportionate effort.

Given these conflicting messages, lenders feel frustrated when there is a sudden, intense policy focus on a new initiative in which their involvement is urgently sought when the overall architecture of housing policy seems hazy. A good market would include a better understood public policy strategy for housing.
"It's difficult for a lender to influence housing supply. But Government's housing supply policy needs to be credible. Home-ownership is still seen as the goal. But lenders can support various tenures. Housing strategy should not be "gimmicky" - there is no benefit in pushing sectors beyond their natural limits. For example, will customers be able buy their way out of shared equity? If not, we should ask whether it is the right solution."

Playing by the rules

Regulators, too, have an important contribution to make. Lenders do not believe that it is within the gift of regulators to create all the conditions that deliver a good market. But they do think that regulators can do several important things that make a good market more likely. They can:

- Make sure that regulation is targeted primarily at protecting the stability of the financial system, as this is in the interests of all financial consumers (as well as their lenders and the UK economy). Prudential regulation is a powerful tool with which to influence lender behaviour, and may result in similar outcomes as detailed conduct-of-business regulation.
- Use conduct-of-business regulation to help lenders avoid real consumer detriment, rather than to eliminate all lending risk. Lenders feel that consumers' interests would be better served if regulators were also more active in reinforcing the "caveat emptor" message, alongside consumer protection measures, as they fear that the principle has been diluted by the "compensation culture".
- Ensure that they are absolutely consistent in their interpretation of rules - both in ensuring that supervision is consistent across different supervisors, in line with the policy intention, and also in ensuring that interpretation is consistent over time, reducing the risk of "regulation with hindsight" in relation to past business.
- Target outliers and police the perimeter of regulation stringently. One problem that regulators and consumers both face is that any tightly regulated market (such as the mainstream mortgage market) creates opportunities for unregulated pop-up alternatives to appear and thrive, until they too fall with the scope of regulation - sometimes well after the horse has bolted. Sale-and-rent-back (SRB) is one example. When SRB itself became regulated, the SRB market disappeared yet "lease options" emerged, and (as evidenced by a recent FSA warning to mortgage brokers) secured short-term/bridging lending is now being seen by some as an alternative to SRB for borrowers in distress. The game of regulatory catch-up is frustrating for all concerned, but essential to protect consumers - the real scams are always likely to be the ones operating just outside the reach of regulation and redress.

"Prudential regulation will influence lender behaviour at least as much as conduct-of-business regulation. I think the MMR will result in over-complication of the sales process and over-values advice. Whoever sells the mortgage, the lender is left holding the baby which ought to be the best discipline on quality."

How lenders see their future contribution

So how do lenders see their future role in the market? Do they expect mortgages to become more or less important to them as a business? Do they expect to be market innovators, and if so how? How do they see themselves relative to other lenders in the market? And what do lenders think that they themselves can do, either individually or collectively, to support a good market?

All the lenders we interviewed expected to play an active role in the mortgage market in future, with none expecting to leave the market and many expecting to become more active. However, some lenders expected mortgages to become less important within their businesses overall, and most expected conditions in the wider economy to be the primary determinant of their future business volumes.
Lenders were very clear that it is public policy, rather than business, that needs to determine the overall thrust of UK housing policy. While many lenders specialise in lending for home-ownership and a few in buy-to-let, virtually all lenders could clearly articulate the "socially useful" function that the UK mortgage lending market performs: it helps to finance the production and acquisition of homes the country needs; it helps individuals to have choices about where they live and whether they buy or rent; and it helps to provide property landlords with finance to enable them to invest in and improve housing. Many lenders were extremely proud of the legacy of home-ownership that the UK mortgage market had helped to create, and most thought that one crucial ongoing objective of the UK mortgage market was to continue to provide lending to help those who aspire to home-ownership, and who can afford it, to achieve it.

Moving on to specifics, lenders offered a range of thoughtful and creative reflections on how they felt lenders could work towards the evolution of a better market overall. For example:

- Many lenders see a case for simplification, at least for some customers

There is a clear trade-off between choice (lots of different products) and simplicity (easy to understand). At heart, mortgages are not fundamentally difficult to understand, but a culture of complexity has sprung up around them, as noted earlier. Many lenders feel we can do more on this as an industry, to supplement the work of the FSA/FCA in terms of disclosure, the Money Advice Service in terms of consumer education, and intermediaries/lender sales staff in terms of point-of-sale information. The CML will explore how it can help lenders achieve this.

- Customers outside the mainstream ought to have niche products available to them - for example, high net worth customers, and the self-employed - but generally speaking for the mass market there should be a smaller number of simpler and more straightforward products.

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- Many lenders see a case for different dynamics in mortgage selling

Distribution is a key area on which the industry needs to do further work with regulators, intermediaries, and consumers. There is a place for advice, and a place for execution-only sales. People who have the job of advising on and selling mortgages need to be paid for their work, but incentives and remuneration - across both direct and intermediary channels - need to be aligned correctly with good outcomes for consumers and lenders (crucially, in both the short and long term). The only acceptable answer to the question: “why did this customer end up with this particular mortgage?” should be "Because it is the right fit for their needs ". Not all lenders are convinced that the current market is unequivocally transparent enough to deliver this outcome.

Sales incentives are one of the features of the wider financial services landscape - not just mortgages - that both the incoming head of the new Financial Conduct Authority and several major UK bank chief executives have talked about recently. And lenders want to ensure that the integrity of distribution is skewed neither by their own internal processes, nor by business-to-business relationships, not all of which are visible to customers. Brokers, packagers (in some areas of the market), panel managers, mortgage networks, valuers, conveyancers and builders could all potentially indirectly influence the choice of mortgage that the non-direct consumer ends up with. So we expect that a focus on enhancing transparency across all aspects of mortgage distribution will be pursued next year.
"Lenders need to move away from a market where the focus is on the sale. We need to consider more regular reviews with the customer and not focus on two-year fixes, which creates churn."

"We need a healthy intermediary market - but there needs to be more focus on quality. Advice can be geared towards compliance more than towards quality. Current remuneration structures for intermediaries focus on the transaction, but need to move towards a longer term perspective."

"We should be clearer about how we can make sure that remuneration throughout the distribution chain - lenders and brokers - works with the interests of customers and not against them."

"The rise of the internet and the ability to compare and shop around online will be a big feature and will benefit customers in the future."

"I think arranging your mortgage online would be becoming normal consumer practice now if it weren't for the mortgage market review and uncertainty about how to deliver its advice requirements online."

• **Many lenders see a case for process innovation**

Innovation in the mortgage market can mean many things, and has at times referred to systems innovation such as automated "desktop" valuations, credit scoring decisioning systems, and "fast track" lending where random cases were spot-checked rather than individually evidenced for income. These devices had their place but became over-used.

Innovation that dilutes good credit assessment is not what our respondents support. And the scope and scale of regulatory change over the next couple of years may make it difficult for lenders to invest in process innovation. But improvements that reduce cost, improve efficiency, or de-duplicate effort are being pursued. Positive kinds of innovation currently under consideration by lenders include individual products that meet niche consumer needs without undermining credit quality; examples would include use of indemnities to offset risk as in NewBuy and the Local Authority Mortgage Scheme, and the streamlining of individual lenders' checks on their business-to-business relationships into a central solution (an industry panel management approach to conveyancers might be an example of this).

"People need to understand the risks of new products. We need to look at new products from a customer viewpoint."

"Innovation will probably come primarily through distribution. Technological developments will have a role to play where they reduce cost or increase efficiency without diluting lending quality. The internet may well become a far more normal way for people to take out mortgages than it has been to date."

"Innovation is really important. But over the next 2-3 years a lot of lenders' resources will be tied up in delivering the changes required by regulatory change, so I think it is unlikely that a great deal of additional change will happen until after that."

• **Many lenders see a case for building products with greater flexibility**

Many lenders can also see the potential to do more to think about flexibility to allow rent-to-buy, staircasing, portability, home-ownership exit strategies, niche areas such as lending for self-build, etc. These could help to support a more fluid market across the fully owned, part-owned, shared equity and private rented sectors.

However, the small scale of these initiatives and their current fragmentation makes work across these markets relatively difficult for lender engagement. More co-ordinated policy action would help more effective engagement. The review of section 106 agreements is a good example of how this can work.
"A product that flexes for consumers would be a good idea...but some of the best funding solutions for mortgages (such as RMBS) are not easily compatible with flexibility for consumers."

"We should introduce products that serve the longer term interests of borrowers and can flex with them. This isn't easy, but there must be ways it can work."

"There are plenty of little schemes out there, but they all have their own bells and whistles and they're all about the size of a whelk stall."

- Many lenders see a case for working with markets and regulators to achieve a more stable funding base

Funding needs to be mixed, and reliable. Most lenders place a very high degree of importance on future funding market conditions as a key determinant of mortgage market conditions. Even those lenders who rely primarily on retail deposits said that the maturity matching risks and liquidity risks available from the wholesale markets are a reason for their having a diversified approach to funding and to their using wholesale sources.

Most lenders are not convinced that structural issues in the funding markets have been sufficiently addressed to deliver a predictable, sustainable mortgage market after government interventions such as the Funding for Lending scheme expire. This can only feed lending caution. This suggests that the lending industry needs to work with the Bank of England, regulators, market investors and lenders to identify how funding markets can operate more reliably and sustainably in the future than they have done in the past. Perhaps there is a window of opportunity to do this during the life of the Funding for Lending scheme.

- Many lenders would like to find ways to solve the high loan to value paradox

Not one of our respondents saw a strong case for widespread 100% LTV mortgages in the house purchase market (although some said that they wanted to have the option to be able to offer them to good existing borrowers trapped with little equity who needed to move home and where the lender's risk would not be increased). But many lenders said that the market was currently too skewed towards lending at up to 60% LTV, with too little lending at higher LTVs. Lenders rightly pointed out that high LTV lending is a long-term market norm for first-time buyers, with mortgages of over 90% having been the average for first-time buyers for three decades, without obvious detriment.

But capital requirements are now - rightly - more stringent on higher LTV lending and high LTV in the past didn't necessarily go hand in hand with high loan-to-income ratios, which is what happened immediately pre-crisis.

"Initiatives such as Funding for Lending can end up creating their own distortions. It's important for the long term to free up the mechanics between lending and borrowing so that the market can function properly without intervention."

"Funding is very important. The structure needs to include a decent amount of wholesale funding. RMBS can be a good structure, and makes more sense than covered bonds in the UK. Government schemes have helped to plug to market funding gap, but also make it more difficult for a stand-alone market to get going."

"Funding is THE big long-term structural issue."

"Funding needs differ from firm to firm - so much depends on what legacy products a lender has. Both retail and wholesale have risks. With wholesale, you are dependent on investors' views of the market and of your business, which can be very transient. Retail savings are increasingly promiscuous, and only as reliable as your rate in a very competitive market. The FSA liquidity regime assumes 70% of retail deposits will be lost on a downside risk, so planning around that is difficult too."
To square this circle, some lenders mentioned the potential for long-term fixed rates to be a responsible market solution for highly geared borrowers wanting high LTV mortgages. But lenders also saw a number of barriers to making long term fixed rates a popular borrowing choice - notably, the culturally embedded lack of value that UK consumers seem to place on certainty (contrasting with a willingness to accept future affordability risk as a trade-off for low initial cost), and the relatively high costs associated with early redemption on fixed rate mortgages, making borrowers fearful of being "trapped". This remains an approach in which some lenders will be interested as part of their overall strategy for longer term products to meet customer needs.

"Without wanting to whinge about capital, the regime does push lenders to undertake low loan-to-value business rather than high loan-to-value business, which doesn't actually reflect consumer needs in the market terribly well."

"The market tends to respond to risk and funding more than to consumer preferences."
Conclusions and next steps

There are already many positives about the UK mortgage market. It underpins the social fabric of the UK and delivers the finance that enables people to own homes, as well as the finance that supports a good quality private rented sector, social housing, and intermediate tenure.

Yet the mortgage market is not perfect; in addition it works within a far from perfect housing market. If both the wider housing market, and the mortgage market that supports it, can be made more resilient, more flexible to changing housing needs and aspirations, and more predictable for the long term, both the UK economy and UK consumers will benefit.

An increased flow of lending to the housing market is desirable to stimulate and support economic growth; but tight regulation to dampen market practice makes lenders cautious. Home-ownership is still the tenure of aspiration, but can it realistically be delivered? If not, what are the best ways for lenders to explore a sustainable business model for lending-for-housing, predicated somewhat less on lending-for-home-ownership?

Clearer answers from government and regulators would help lenders to plan their future services.

However, lenders also recognise that there is plenty that they can do for themselves and their customers to deliver what many see as the characteristics of a good market.

Taken in the round, the following steps are examples of those that might logically follow from the results of the self-evaluation, to safeguard a "good" mortgage market for the long term, for both lenders and borrowers.

Lenders would:

- Work towards redefining their relationship with customers so that it more often leads to a longer-term service centred on the customer's evolving needs, not simply a single and sometimes short-term transaction.

  "Restore trust and integrity in the sector by building things around consumer needs rather than around lender processes."

- Review their product set so that it is simpler to understand, and communicate with as much clarity as possible about the trade-offs between risk, pricing, rates, fees, and charges, to empower customers to understand the choices being made.

  "Align lending behaviour with consumer interests - decisions to lend demonstrably need to be based on the consumer's circumstances, rather than on the lender's desire to grow."

- Streamline their processes without sacrificing rigour for cost saving so that they are user-friendly and slick – and potentially easier for consumers to understand.

- Make distribution – by whatever channel – work for their customers with an unequivocal focus on their best interests.

- Share and benchmark good practice.

  "Improve our industry-wide ability to benchmark good practice."
• Work toward delivering products that are flexible enough to cope with shifting consumer needs and adaptable to different expectations for customers' housing options.

"Move away from a manufacturing environment to one where there is more relationship management between lenders and borrowers. Recognise that sales incentives change behaviour."

But creation of the good market also has implications for others outside the lending industry.

Regulators would:

• Be prepared to offer consistent interpretation of rules, especially when the regulator's precise intent is ambiguous/unclear. This would reduce the unintended consequences risk both of inadvertent non-compliance, and of ultra-conservatism, on the part of lenders - neither of which match regulatory objectives.

"I would favour voluntary industry initiatives or codes that deal with issues at the edge of the regulatory playing field."

• Recognise the best ways in which to influence behaviour in the market – which may be through prudential regulation, or conduct regulation, but where double-layering both prudential and conduct rules may be unhelpful.
• Be prepared to modify their rules quickly if they are perceived to deliver unintended consequences.
• Not duplicate regulation in a way which adds unnecessary complexity to compliance.
• Take into account ways in which lenders mitigate their risk in the imposition of capital requirements, especially to encourage higher loan-to-value lending.
• Recognise the role of competition as a regulatory tool.

Government would:

• Decide whether or not it continues to have an aspiration towards increasing home-ownership, or whether it sees its role as managing a transition to lower levels of home-ownership, and craft its housing policy accordingly.
• Focus on an over-arching housing strategy, across all tenures, and join up currently disjointed initiatives.
• Simplify and standardise mechanisms for intermediate housing and other niche areas so that the effort required for lenders to engage with them becomes more proportionate.
• Engage with lenders more actively to understand the mechanics of lending and the practicality of delivering Government objectives before future announcements are made.
• Focus on the encouragement of new build to help address the long-standing imbalance of housing supply and demand.

As for the CML, our work programme in the coming year will reflect support for the lenders in delivering on the practical steps implied by this project; and in encouraging the other parties to address the parts which they need to play. We intend to:

• Help the industry identify how products can be simplified and made more flexible;
• Discuss with intermediaries what relationship between lender and intermediary can best deliver a good market for consumers;
• Continue to press regulators for reasonable and pragmatic implementation of MMR and other regulatory initiatives; and
• Create a better means of benchmarking best practice.