INTERNATIONAL UNION FOR HOUSING FINANCE
FACT SHEET

> UNITED KINGDOM

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1. DEMOGRAPHIC OVERVIEW

The UK has approximately 62 million inhabitants. A third (33%) are aged between 21 and 44 years, a quarter (25%) are aged between 45 and 64 and another quarter (25%) are under 21. It is expected that the group over 65 years old will steadily increase in the coming years, thereby increasing the demand for housing stock adapted for the elderly.

The pressure on housing demand will also arise from two other sources. The first relates to the fact that over the last five years the UK has had an average annual population increase rate of 0.64%. The increase in population will raise the demand for housing, particularly given the increasing trend of one person households. The second source of pressure on the housing market comes from the net migration rate of 2.15 per 1,000 inhabitants that the UK receives annually, which also needs to be accommodated.

2. MACROECONOMIC BACKGROUND

While the UK economy grew strongly between 2005 and 2007, at an average real GDP growth rate of 2.6%, once the global financial crisis hit the country, the economy suffered an intense slowdown leading to a negative GDP growth rate in 2009 (-4.9%). The UK was particularly affected by this crisis given its position as a key global financial centre.

The decrease in growth was accompanied by a slight increase in the unemployment rate from 4.9% in 2005 to 7.6% in 2009, distancing itself from its twenty year low in 1999 (4%), and by a large reduction in the real fixed investment in housing growth rate, reaching -17.7% in 2009. Nevertheless, these changes did not seem to have a significant effect on the consumer price index, which, over the last five years, has remained basically stable at an average rate of 2.5%, except in 2008 when it increased slightly,[1] or the median gross annual pay which steadily increased from GBP £18,950 in 2005 to GBP £21,320 in 2009.[2]

The service sector, which includes the financial services sector (i.e. banking, insurance, etc.), represents 75% of Gross Value Added and accounts for 83% of the country's labour force. In part this explains why the financial crisis very quickly turned into a recession in the UK. Despite the fact that the agricultural sector only accounts for 1% of the GVA and 2% of total employment, this sector is highly efficient according to European standards. In contrast, the importance of the industrial sector in the economy has been declining over recent years and, although the UK has coal, natural gas and oil resources, the country became a net energy importer from 2005.

[1] According to the EMF's Hypostat 2008, "because this relatively high inflation was largely the result of a spike in energy prices it was temporary in nature".
[2] Note that, given the fluctuations in the exchange rate between the Euro and the British Pound over the last three years, when the median gross annual pay is calculated in Euros the result is that this indicator has, in fact, decreased from 27,870 EUR in 2005 to 23,560 EUR in 2009.

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3. HOUSING MARKET

3.1. Housing Supply

The UK has approximately 27 million dwelling units, of which around 38% were built before 1945 and only 16% were erected after the mid-1980s. On average 225,000 dwellings were started annually between 2005 and 2007. However, given that the financial crisis had a dramatic impact on UK housing activity, the number of dwellings that began to be constructed almost halved in 2008 (134,000). The same pattern was observed regarding house completions, where an average of 216,000 dwellings were completed before the crisis and then this average dropped to 183,000 in 2008. The crisis also affected residential house prices. In 2008 prices declined strongly for the first time since the early 1990s, reaching levels lower than those recorded in 2005. Prices somewhat recovered after the first quarter of 2009.

3.2. Housing Tenure

The UK has one of the highest ownership rates in Europe, where 70% of the housing stock is owner-occupied and, out of which, 45% currently have no mortgage loan to repay. Despite the fact that homeownership has been increasing over the last 25 years, recently this trend seems to have slowed down. Following the housing boom in the mid-2000s, many households could not afford to buy a home and nowadays, in the wake of the crisis, problems in gaining access to credit are still affecting house purchases.

Since the 1980s, the number of people renting has been steadily increasing. The UK is one of the most liberalised private rental markets in Europe and 12% of the country's housing stock is currently rented from private landlords. However, this may change following the new housing policy of the current government which has stated its aim to increase homeownership.

Although in the 1980s local authorities or registered social landlords (RSLs) held approximately one third of the UK's housing stock, nowadays they only own 18%. The reason for this reduction is due to the increase in new building construction coupled with the sale of around 2 million dwellings to their tenants. Much of this stock is mainly rented out to lower income groups and immigrants.

4. RESIDENTIAL MORTGAGE MARKET

4.1. Lending

Mortgage lending in the UK experienced an unprecedented decline from the start of the credit crunch in 2007 until the second quarter of 2009. The reasons for this are twofold. First, securitisation and other wholesale markets closed (although these began to reopen gradually throughout 2009). Second, the unfavourable macroeconomic environment reduced demand for mortgage loans.

From the second quarter of 2009 the lending market stabilised and observed a moderate recovery mainly based on the slow growth of house purchases, though the remortgaging market continued to decline. Increased transactions, mortgage lending and house prices were results of low interest rates and the temporary exemption on the stamp duty tax for dwellings priced between GBP £125,000 (EUR €140,000) and GBP £175,000 (EUR €196,000) until the end of 2009.

Low interest rates and a smaller than predicted increase in unemployment explained the moderate increase in repossessions in 2009, which eventually amounted to 47,800 (7,800 more than in 2008) according to the Council of Mortgage Lenders, which earlier in the year had predicted 75,000 repossessions. Borrowers in trouble also found help in support measures that were significantly different from those applied in previous arrears cycles, coming both from lenders, through forbearance, and from the government, via the Mortgage Rescue Scheme, the Homeowner Mortgage Support and the Support for Mortgage Interest programmes.

Residential mortgage debt to GDP is currently 85%, which, despite the crisis, has increased over the last five years. The average loan to value (LTV) ratio decreased to 73.8%.

In the UK, mortgage loans are offered by universal and commercial banks, cooperative and mutual credit banks, building societies and other specialised lenders. Traditionally, these firms have mainly offered

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variable rate mortgages. However, following the crisis there has been an increase in initial fixed rate mortgages, where the mortgage rate is fixed for the initial years and then becomes variable afterwards.

4.2. Funding

The credit crunch had a dramatic effect on the mortgage market in the UK, especially given that over the course of time lenders had generally become more reliant on money markets for funding and far less dependent on retail deposits. In order to ease this situation and maintain confidence in the banking system, the government put in place two schemes: the Bank of England's special liquidity scheme (SLS) and the Treasury's credit guarantee scheme (CGS). The first closed in early 2009 and the second in late 2009. Given that both schemes are no longer active and that the market has not yet fully recovered, some lenders have doubts regarding the feasibility of repaying the SLS and CGS in the timeframe proposed by the government.

Funding for lenders in the UK comes from retail deposits, residential mortgage backed securities (RMBS), covered bonds and other wholesale sources. Following the crisis, private securitisation seemed to have come to a halt for a period of time. However, in the autumn of 2009 it resumed with somewhat different characteristics than before the crisis, as two of the largest lenders started to launch new issues including a put option by which investors could sell the bonds back to the lender after a period of five years. This formula made these new issues closer to covered bonds than traditional securitisations. In parallel, it is interesting to note the increase in the number of new issues of mortgage bonds from GBP £8 billion (EUR €11 billion) in 2005 to GBP £83 billion (EUR €105 billion) in 2009.

5. GOVERNMENT HOUSING POLICIES

The new Coalition Government is likely to bring in new housing policies and introduce changes to mortgage market regulation and legislation. Consultations on new regulation continue: the Mortgage Market Review, Changes to Regulations for Arrears Handling, Mortgage Repossession Protection of Tenants Act 2010, Homeowner & Debtor Protection Act Scotland 2010 are currently being discussed. Already, Home Information Packs have been suspended.

Until the proposals mentioned above are adopted, the situation with regards to government housing policies is as follows. There is no tax relief on mortgage interest for owner-occupied housing, although capital gains are tax-free. There is a stamp duty tax on transactions above GBP £125,000 (EUR €140,300), GBP £250,000 (EUR €180,600) for first-time buyers, although in disadvantaged areas this tax is at times exempted. Finally, there is no VAT on new dwellings, but VAT of 17.5% applies to all expenditure on home improvements.

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