Changing agenda

The return of 100% mortgages and the rise of later-life lenders herald an evolving UK RMBS landscape. **Claudia Lewis** investigates.

The UK RMBS landscape is set to evolve in the coming years as new mortgage products emerge. Indeed, the return of 100% LTV mortgages and the rise of specialist later-life lenders in the jurisdiction nod towards a more socially-focused agenda, as they seek to address borrowers' changing needs.

The revelation in May of Skipton's 100% LTV mortgage product promises assistance to first-time buyers seeking to get onto the housing ladder in the UK, following the withdrawal of the government's help-to-buy scheme *(SCI 6 April)*. However, the lender has received some criticism for marketing 100% LTV mortgages again post-GFC, as fears return over the issue of negative equity.

"There's not much difference between a 100% mortgage and a 95% or even 90% mortgage, to be honest with you," understands Tom Ward, partner at TLT.

"Everybody gets so frightened of negative equity, which is only really a systemic concern where you have high unemployment coupled with rising interest rates," adds TLT partner Mark Thomas. "We've got over-capacity in employment, no pressures on unemployment rates and so a first-time buyer with a very reasonable and conservative income multiple on a small loan on a small property in a 100% employment scenario isn't that risky. If it's not miss-sold and it's done on an ethical basis, there's clearly room for a product like that in the market – and I don't see that it's really any different to any other regulated owner-occupied mortgage."

In fact, the offering from Skipton is relatively low risk, as the lender is set to offer its 100% mortgage product only to a distinct group of borrowers earning between £95,000 and £100,000 a year – which excludes a large proportion of ▶


Arjan Verbeek, Perenna

continues to near market entry. "Whatever your background is, you look at us slightly differently," explains Verbeek. "People that don't work in finance see us as a bank that does mortgages, whereas if you're an RMBS expert, you would probably see us as a master trust with a banking license."

He adds: "The advantage of our model – a covered bond bank – is that you can issue long-dated fixed rate bonds, which has the right treatment in the market and is accepted by regulators and investors. And they have massive advantages for people who can't currently get a mortgage; that's the key thing."

how much they can borrow. "If you go to another bank's calculator, you will simply get a multiple – for example, 3.5 times your income. But ours actually calculates how much you can afford," Verbeek states. "It doesn't matter whether you earn £25,000 or £100,000, young or old – if you can afford the debt, we will give it to you."

However, the firm faces a significant regulatory block by government. Verbeek explains: "Unfortunately, the financial policy committee is not allowing this at the moment because we can only give 15% of people more than 4.5 times their income. So, the Bank of England forces us to say

> "TO GET BETTER CAPITAL MARKETS, YOU NEED TO HAVE FAIRLY PRICED MORTGAGES, AND THE BANKS NEED TO BE FORCED TO PRICE THOSE MORTGAGES COMPETITIVELY"

struggling first-time buyers. "I think it's a very sensible product to try and get people out of the rental trap without adding further risk – enabling people to get on the property ladder," considers Thomas. "Crucially, they're not lowering the criteria; whereas, if we were to see the criteria being relaxed substantially, then I would be more concerned."

The UK government has been criticised for not promoting the need for young people to enter the housing market, as neither regulation nor structures have been set up to support this. However, 100% mortgages may be an important first step.

Expanding into the underserved mortgage demographic is not only important for those customers, but also for the future of the UK's mortgage market – which was ranked in last place in Fitch's recent assessment of 10 mortgage markets.

"To get better capital markets, you need to have fairly priced mortgages, and the banks need to be forced to price those mortgages competitively," notes Arjan Verbeek, founder and ceo of Perenna.

Kerr argues: "I do think these are the sort of products that are better served to come from a building society where they have a lower cost of capital, as their model will be able to offer those products at a more reasonable rate than a high street lender necessarily would."

A 95% LTV mortgage product for UK borrowers has since been announced by Nationwide, while a long-term fixed 100% LTV offering from Perenna

Perenna is planning to offer 30-year fixed 100% LTV mortgages – which have already been offered elsewhere in Europe and successfully securitised, including in Obvion's Green STORM transactions. "The Netherlands has always been a high-LTV market, but they are also different to the UK in terms of the fixed rate term which is offered," says Gordon Kerr, head of European research at KBRA.

Kali Sirugudi, structured finance analyst at KBRA, adds: "And it's these high LTVs and longer fixed rates that works for the borrower."

In fact, the fundamental critique is of the product's five-year fixed structure, which exposes borrowers to remortgage risk and the risk of negative equity. Sirugudi asks: "Will Skipton be able to offer a remortgage product to such existing borrowers who have fallen into a negative equity position?"

Perenna has recently made available its own mortgage calculator to show customers exactly

to one person 'yes' and another person 'no', which is complete discrimination."

According to Perenna's newly launched mortgage calculator, a 30-year-old first-time buyer earning £100,000 before tax a year could borrow a total of £513,640 for a 95% 35-year fixed mortgage. This compares to the £600,000 figure Skipton quoted as being able to lend first-time buyers.

The path forward, given the future success of Perenna's long-term fixed 100% mortgage products, may see several more companies following its lead – to which Verbeek takes no issue. "Once we are up and running and we have people, we show people it works and how it works, I have no doubt that people will be looking to clone us."

He continues: "Denmark has four or five covered bond banks, as does Germany – it's not a problem, it's actually very good for the market. We need to get to a fair mortgage market that works for everybody; not the one we currently

Gordon Kerr, KBRA

have, which is dictated by six or seven lenders at a cheap price, just to roll people in and make money from other parts of the business. That's not a healthy economy."

"If we get a better priced mortgage market, we will also see an increase in capital markets activity – which isn't happening at the moment," Verbeek adds.

Sufficient origination volume is fundamental to the inclusion of these mortgage products from specialist lenders in RMBS pools. "From an individual lender, you're not going to get to the size and scale that would solicit a purely social securitisation structure," explains Kerr. "But what you may find in the end is that they may try to contemplate pool products, such as the 100% LTV and later life products."

It will likely take some time before 100% LTV mortgage products enter RMBS pools, which Thomas expects to see as the minimum earning criteria of £95,000 to £100,000 reduces – enabling the creation of decent sized portfolios. "But I wouldn't be surprised if you see them going into other portfolios or mixed portfolios and being part of the overall blend around 75%, but I think it will take time. I think in the meantime you will have more private sales, more forward funding, more private securitisations – which will be testing between lenders where the market is, where the value is and therefore where the arbitrage value is on the RMBS."

Specialist lenders in the UK are also expanding into later life mortgage offerings, as current equity-release products arguably don't serve the best interests of elderly borrowers. Lenders, including LiveMore Capital, have been established to specifically target this demographic.

"If you are renting in retirement and don't own your house, you need to have a pension pot that is £360,000 more than if you do," explains Verbeek. "People are already not saving enough of their income for retirement, so this is something that young people also really need to start thinking about."

Kerr adds: "The later life product is not just catering to that particular niche, but is also seen to be catering to the issue and phenomenon of mortgage prisoners in the UK."

There are an estimated 900,000 mortgage prisoners in the UK.

LiveMore has ramped up originations and, with the publication of its social bond framework, is hoping to see loans securitised with ESG labels in the future.

"The FCA is in consultation with many lenders in the UK. They too expect that the retirement interest-only product is absolutely the right one for the purpose of providing relief to the mortgage prisoners who possibly got into house purchase before 2008," Sirugudi explains.

He concludes: "There are certain regulatory and legal-related hurdles lenders have to jump over to take care of these later life products. But once these boxes are ticked, they certainly can cater to this niche."

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CONSUMER DUTY EYED

TLT partner Mark Thomas attests to the FCA's new Consumer Duty rules being a key driver of activity in the UK mortgage market at present, The initial phase comes into force on 31 July, followed by a second phase scheduled for July 2024.

"However, the FCA has made it very clear that it's not waiting for those phases to come in before they're expecting better consumer outcomes – so lenders are already having to get themselves up to speed," explains Tom Ward, partner at TLT. "As there are specific obligations within it that apply to the buying and selling of portfolios, would-be sellers are having to make sure their books are compliant before they sell and buyers are being obliged to ask for information which sellers are having to make sure they have at their fingertips."

In instances where a buyer purchases a portfolio that does not conform to the FCA's guidelines, they won't be able to securitise it. However, the rules do not yet offer any concrete details as to their application in respect of RMBS.

"There are concepts and structures typically seen in RMBS, like the split of legal and beneficial title, which are not expressly covered in the rules and guidance around consumer duty at present. Also, what happens if there's a mix of regulated and unregulated entities and outsourcing arrangements within an RMBS structure? Who is responsible for what in that scenario?" asks Ward.