

October 2015

## FCA Call for Inputs on Mortgage Sector Competition

On 7 October 2015, the FCA published a Call for Inputs on competition in the mortgage market. It provides an opportunity for those with an interest in the sector to help identify, in particular, potential areas where competition in the interests of consumers may not be working well and could be improved (or conversely if competition is working well).

This activity is driven by several key concerns:

- Questions about market dynamics, including in relation to specific market segments or groups of consumers;
- The fact that some issues might become more acute over time - for instance, in the event of changes to the economic environment such as interest rate rises;
- Recent regulatory changes, including the Mortgage Market Review (MMR), and the regulator's interest in assessing its impact on the market; and
- The FCA's wider programme of work on mortgages, including the recently completed Advice and Distribution review and the ongoing Responsible Lending review.

**Next steps:** the FCA are asking interested stakeholders to respond by 18 December, with a view to publishing a feedback statement in the first quarter of 2016 summarising the analysis of the responses received and setting out any further action.

### Overview

On 7 October 2015, the FCA published a Call for Inputs on the mortgage sector competition, forming the first stage in review into barriers to competition in the mortgage sector.<sup>1</sup>

### Background

The FCA has been has an operational objective to promote effective competition in the interests of consumers in financial services. Following the implementation of its Mortgage Market Review (MMR) in April 2014<sup>2</sup>, the regulator has been monitoring implementation and published a review earlier this year on implementation of advice and distribution. The present review looks at barriers to competition in the mortgage sector and was announced in the FCA's Business Plan 2015/16. The decision to undertake this review is based on several factors:

- Questions about market dynamics, including in relation to specific market segments or groups of consumers;
- The fact that some issues might become more acute over time - for instance, in the event of changes to the economic environment such as interest rate rises;

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<sup>1</sup> <http://www.fca.org.uk/news/call-for-inputs-competition-mortgage-sector>

<sup>2</sup> Financial Conduct Authority Thematic Review TR15/9: Embedding the Mortgage Market Review: Advice and Distribution, 9 July 2015. [www.fca.org.uk/news/tr15-09-embedding-the-mortgage-market-review-advice-and-distribution](http://www.fca.org.uk/news/tr15-09-embedding-the-mortgage-market-review-advice-and-distribution)

- Recent regulatory changes, including our Mortgage Market Review (MMR), and the regulator’s interest in assessing its impact on the market; and
- The FCA’s wider programme of work on mortgages, including the recently completed Advice and Distribution review<sup>10</sup> and the ongoing Responsible Lending review.

## The competition review process

In prioritising issues for any such market study, the FCA has said it would bear in mind the following:

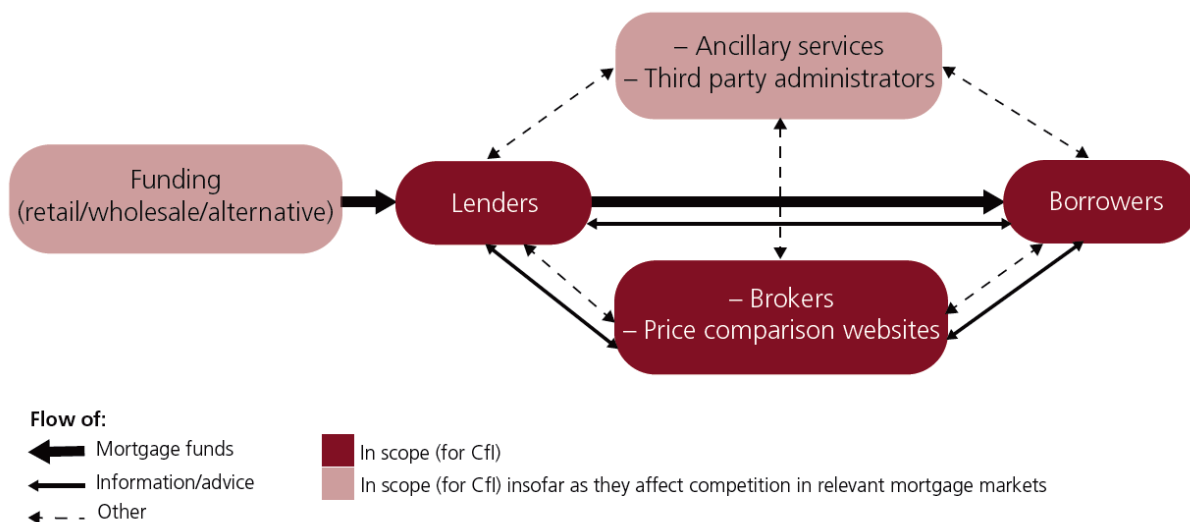
- The prospects for, and likely impact of, any intervention. This will be a combination of:
  - The potential impact of intervening to address the issue in question;
  - The scope to intervene effectively (considering, for instance, the role of other national and international regulators); and
  - The prospects for the intervention to have a wider impact (for example, through deterrence effects or clear read-across to other markets).
- How the issue in question fits in with any upcoming regulatory developments/ongoing activity at a domestic, EU or wider international level;
- Whether market changes or forces are anticipated in the future that might serve to address any issues identified;
- How a market study would affect the FCA’s current portfolio of work, including any resource implications;
- Whether the issue might be better addressed by another form of FCA intervention (such as supervisory or enforcement action), or by another authority; and
- The likelihood of a successful outcome (in terms of being able to intervene to make the market work better for consumers).

The regulator will publish, in the first quarter of 2016, a Feedback Statement summarising our analysis of the responses received and setting out any further action.

## Scope of review

The mortgage sector is defined as the range of markets for the provision of loans secured against a property, encompasses both regulated and unregulated activities. It includes, for example, lifetime mortgages, shared ownership, buy-to-let, second charge mortgages and bridging loans.

### Scope of Review (FCA diagram)



## Assessing competition in the mortgage sector

The call for inputs also sets out the FCA's approach to assessing competition in this sector, and lists some examples of competition issues that could lead to consumer detriment:

- Consumers may buy mortgage products or services which are inappropriate for their individual needs and circumstances. For example, consumers might take up mortgages with significant early repayment charges when they are likely to need to terminate their contract in a fixed rate period;
- Consumers may pay too much for the products or services they receive. This might take the form of high costs (including product fees or commission) or poor value in terms of service standards; and
- So-called 'missing markets', where there is a genuine consumer need that, for some reason, which may include regulatory barriers, nobody comes forward to supply. For instance, some (credit worthy) borrowers may be denied access to mortgage finance, or prevented from switching to products which better meet their needs and circumstances.

Detriment could stem from either supply or demand-side behaviour:

- Demand side behaviour, focusing on whether consumers can effectively access, assess and act on information about mortgage products and services;
- Supply side behaviour, including: how firms reflect consumer behaviours and biases in their pricing and product design decisions, eg whether any businesses have market power in all or segments of the sector, whether there is any evidence of, or scope for, co-ordinated behaviour or the nature and impact of vertical relationships (including potential conflicts of interest).
- Market features, particularly in relation to the impact of the regulatory regime (including specific changes introduced following the MMR), and barriers to entry and expansion or innovation.

## Potential areas of interest for the FCA study

### Demand-side (consumer) issues:

Consumer must be able to access complete, relevant and accurate information about mortgage products and services, use the information that they gather to assess, in an informed manner, those products and services and whether they are likely to meet their individual needs, circumstances and preferences; and act to purchase the service or product they have identified as being the best fit (or choose not to purchase, if that is in their best interest).

- Use of information gathering / comparison tools
- Restrictions in service or product offerings
- Additional challenges for specific consumer segments and/or those with non-mainstream needs: some types of mortgages, such as lifetime mortgages or mortgages for self-built properties, are offered by far fewer providers than mainstream first charge residential mortgages and tend to be targeted at niche groups
- Ability to assess information: mortgage choice is complex and requires consumers to assess a complicated set of variables and circumstances. Some of the complexity arises from the uncertain environment in which a consumer makes the mortgage purchase decision, including lack of certainty about (but need to factor in) changes to personal circumstances or the wider macroeconomic outlook. But complexity may also arise as a result of product design (for instance, in the form of multi-levelled fees and charges).
- Transparency of fees and charges
- Consumer behaviours: such as focusing on headline rates rather than other features; focusing heavily on initial monthly repayments without considering longer term implications and risks; expressing concerns about 'being locked in' to longer term fixed rates and 'missing out on better deals'; and making assumptions that a similar

range of products and rates will be available to them in the future, and/or that their personal and financial circumstances will have significantly improved by the time they seek their next product

- Role of mortgage advice
- Ability to act on information to make effective mortgage choices
- Switching costs
- Inability to access products

### **Supply side (firm) issues**

- Reactions from firms to consumer characteristics and behaviours;
- Coordination between firms;
- Relationships between firms leading to constraints on firm behaviour; and
- Ownership structure and/or relationships between firms potentially leading to conflicts of interest, or misaligned incentives.

### **Next steps**

The FCA are asking interested stakeholders to respond to this call for inputs by 18 December, with a view to publishing a feedback statement in the first quarter of 2016 summarising their analysis of the responses received and setting out any further action.

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