mes2024
annual mortgage
efficiency survey

New Horizons

Mortgage Efficiency Survey 2024

Contents

Foreword

Welcome to our 2024 Mortgage Efficiency Survey - our 13th edition but our first as part of MSO Software Ltd, a new entity backed by Bain Capital to service the UK's mortgage market, alongside Bain's investment in finova.

This is an annual study into how lenders use technology across the mortgage journey. Many outside the industry generally consider all lenders to be the same – as if they are some homogenous mass. Nothing could be further from the truth, as our conversations with a record 46 lenders reveal.

While lenders face very similar issues, the size and breadth of their toolkit to address them varies considerably. This helps explain some of the differing views we heard when discussing key issues including the impact and implementation of consumer duty, one of the most significant regulatory changes to lenders' operating environments since the dawn of regulation in 2004.

Equally, approaches to the issues surrounding AI, green lending, cyber security, and priorities for the future rarely elicited wide consensus. It makes for fascinating reading.

Thank you to everyone who took part in this study and to those of you who reference it. As always, we hope it helps you better understand the market and your place in it.

Steve Carruthers
Business Development Director

About this report

The Mortgage Efficiency Survey looks at how lenders use technology to support the origination and writing of mortgage business, attempting to uncover the issues affecting and defining efficient lending. It is an annual investigation to understand the shared experience among lenders and the different approaches lenders use to deliver their objectives.

The report allows participants to look beyond their businesses and contextualise their performance in the wider market. Our research examines the lending process from sales through origination to completion and the business and technology issues that impact lenders' ability to administer that journey efficiently.

Scope

This paper aims to lift the veil on how technology issues, and automation, can impact lenders' mortgage processing across affordability, DIP, application, offer, post-offer and completion. This includes product launches, withdrawals, and criteria changes.

To build a picture of the industry over time, we maintain our definition of 'mortgage efficiency' in originating and writing loans. We do not look specifically at post-completion servicing elements such as redemptions or arrears though their impact is recognised in discussions.

Methodology

We interviewed forty-three lenders representing every type of institution, whether by organisation type, balance sheet size, lending market or business model.

The 45-minute video-conference interviews were qualitative, and this approach allowed for a more open dialogue. To get a frank appraisal of lenders' positions, thoughts and views, interviews were conducted under strict anonymity.

Scores reflected not only the perceived experience of the firm but, crucially, the experience and expectations of the individuals who participated. While we welcomed familiar faces during our fourth interview style survey, we also spoke to new responders. As in previous years, some people had left their organisations, or been promoted or retired, meaning some lenders' interpretations and perceptions of their performance over the period differed, reflected in the scoring process. Many interviews included more than one respondent, while other single more senior respondents often 'spoke for' colleagues with specific responsibilities for areas such as operations or underwriting.

Occasionally some who scored their organisations lower were in firms that were comparatively further ahead of their peers but had higher expectations of automation. Nevertheless, the same areas of shared experience and frustration were raised repeatedly, even if responses, priorities, and solutions were more specific at an organisation level.

Introduction

Creating our peer groups

Participating firms were placed in peer groups to help lenders understand their place among similar firms, providing an overall picture and a more nuanced insight into lenders' issues, strategies, and solutions

We have maintained these peer groups so that, where appropriate, we can record and see any trends over the two years. Lenders' peer groups were established at the time of research.

High-street lenders

Typically banks and building societies lending over £4bn per annum, wholesale and retail funded, established with some legacy technology.

Large Societies

Typically larger Building Societies with gross mortgage lending over £1bn but under £10bn per annum, retail funded only, with some legacy technology.

Challengers and Specialists

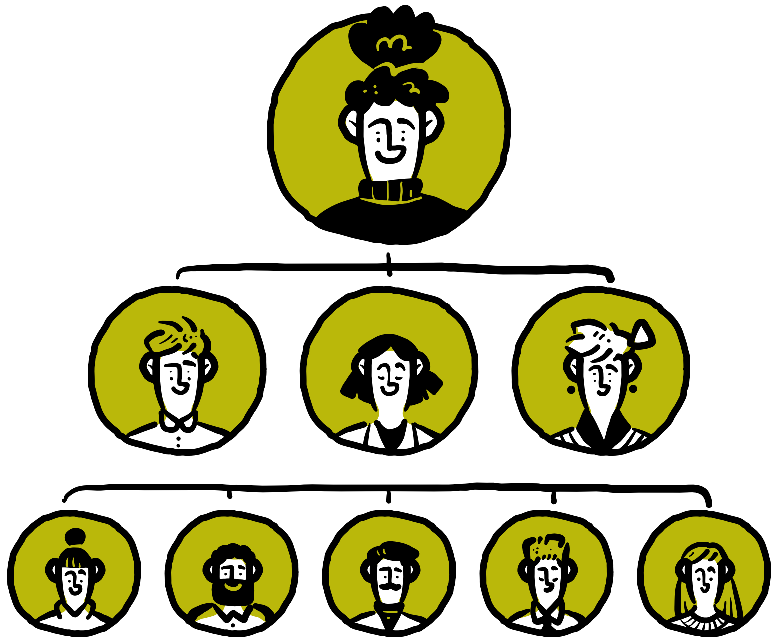
Typically younger institutions with under £1.5bn of annual lending, wholesale or retail funded, and fewer legacy technology issues.

Small Regionals

Typically smaller Building Societies lending under £1bn per annum, retail funded and with legacy technology issues.

Areas of enquiry

Our first questions covered the mortgage origination to completion process. For the most part, lenders shared 2023 data, though occasionally offered rolling year data to the end of Q1 2024. Our final questions focused on what issues are front of lenders' minds and how they impact their businesses.



01

The shadow of affordability hangs over the market

Inflation hits homes

2023 will be remembered as the year that heralded the inexorable rise in inflation, with the Consumer Price Index (CPI) reaching 10.4% in February 2023. The increase was the highest annual inflation rate since March 1992..

This rise brought serious ramifications for UK borrowers. The subsequent hike in interest rates and cost-of-living crisis meant many home owners who were rolling-off deals sold when rates were at historic lows endured significant payment shocks. The higher cost of debt meant that the mortgage market meant that the mortgage market in 2023 challenged lenders, borrowers, and brokers as they all endeavoured to find their feet in the new lending environment.

The impact on affordability drove a weaker mortgage market in 2023. But while many anticipated the same pressures would hold back lending in 2024, the first six months of the year saw growing optimism—partly because of anticipated cuts in base rates owing to improving headline inflation numbers. Expectations of rate cuts and improving swap rates set the tone. A series of cuts were initially priced in for the summer. One materialised in August with hopes of a further cut in the latter part of 2024.

But back in 2023, the increased cost of living, coupled with higher mortgage interest rates, led to a sharp fall in mortgage lending across all sectors.

The number of loans made to first-time buyers in 2023 was the lowest since 2013, down 22.4% on 2022[1]. But home movers were hit even harder, with loan numbers falling by 26%. The 251,000 loans to home movers last year were the lowest figures since 1974[2].

By the time we conducted our interviews in May and June, the market was healing. Notwithstanding the upward repricing of home finance in the face of the growing realisation that interest rates may not come down until the Autumn, buyers and owners were again active in the market though some slowing of activity had begun as the General Election was called, the sun came out, and Euro 2024 got underway. By June, the FCA reported that the outstanding value of all residential mortgage loans decreased by 0.1% from the previous quarter to £1,654.9 billion, and was 1.4% lower than a year earlier and that the value of gross mortgage advances decreased by 2.6% from the previous quarter to £51.6 billion, the lowest since 2020 Q2, and was 12.0% lower than a year earlier[3].

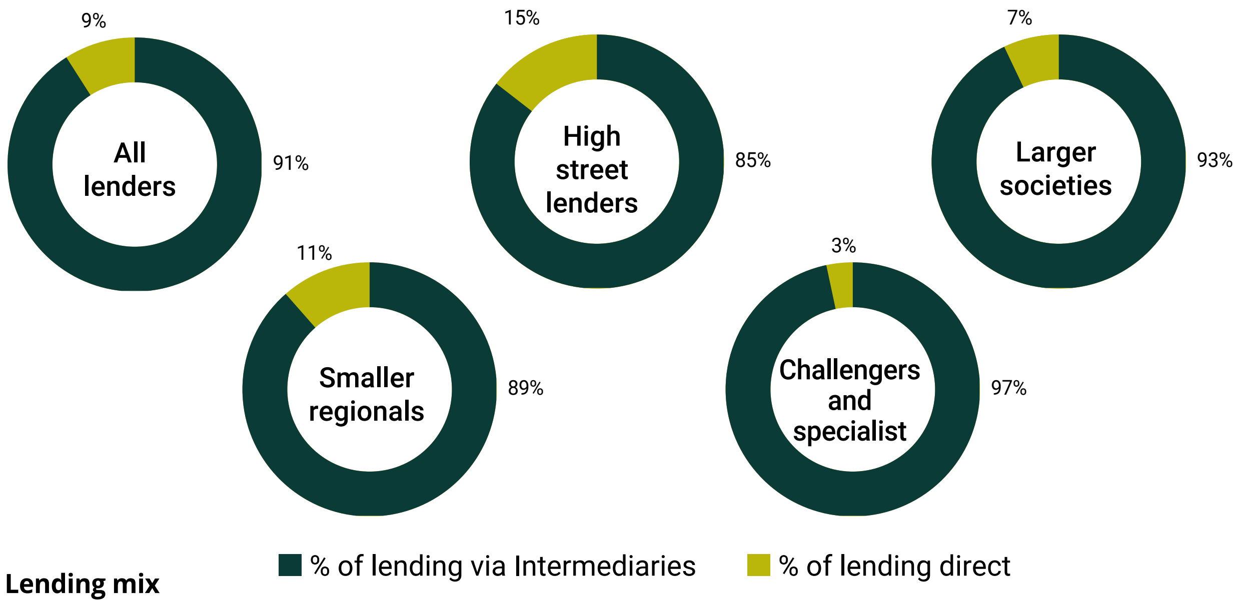
The story of 2023, largely started in Autumn 2022 by the infamous mini-budget, has evolved significantly in the early part of 2024 as headline inflation has cooled. But that battle to contain inflation is far from over.

[1] https://ukfinance-newsroom.prgloo.com/news/affordability-pressures-push-down-mortgage-lending-and-savings-in-2023#:~:text=Over%20the%20whole%20of%202023,22.4%20per%20cent%20on%202022.
[2] https://www.ukfinance.org.uk/system/files/2024-03/Household%20Finance%20Review%202023%20Q4.pdf
[3] https://www.fca.org.uk/data/mortgage-lending-statistics

Distribution splits

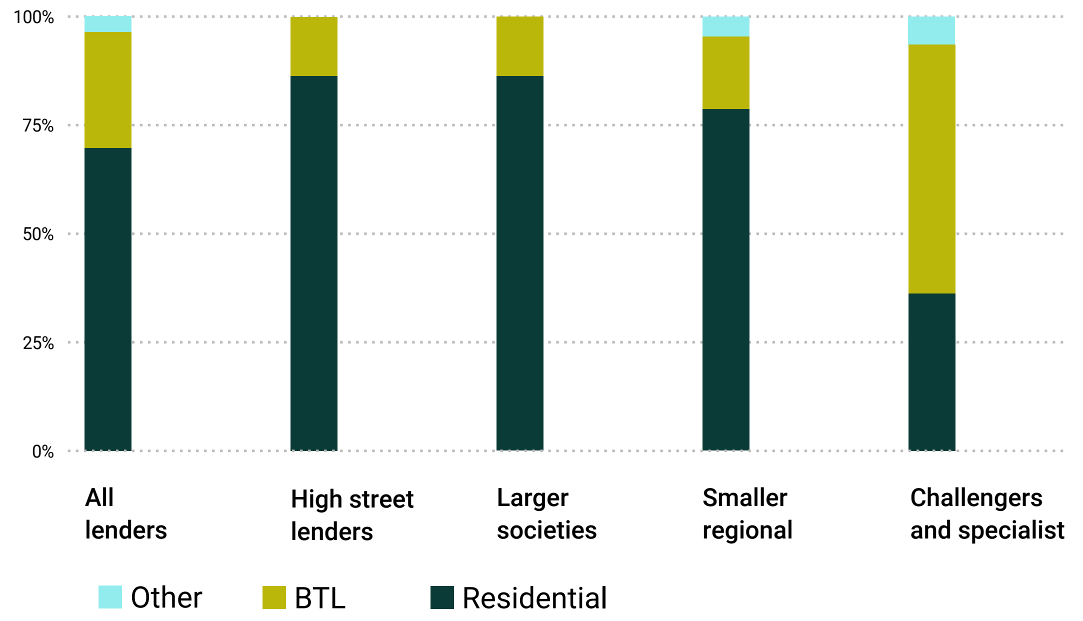
Lenders continued to rely upon broker distribution, with 91% of applications being sourced through intermediaries—a very marginal uplift from last year's figure of 90.9% and remaining above 2022's figure of 88.2% and 2021's figure of 90.3%.

There are good reasons to expect the intermediary market share to remain at this level. Broker distribution is far easier to turn on and off in a volatile pricing environment, and it also de-risks some of the exposures to regulatory risk. Borrowers, too, need good advice from individuals and firms that can access a broad palette of product options, which may include specialist propositions, and that can ensure that protection products are offered to borrowers at times of pricing stress.



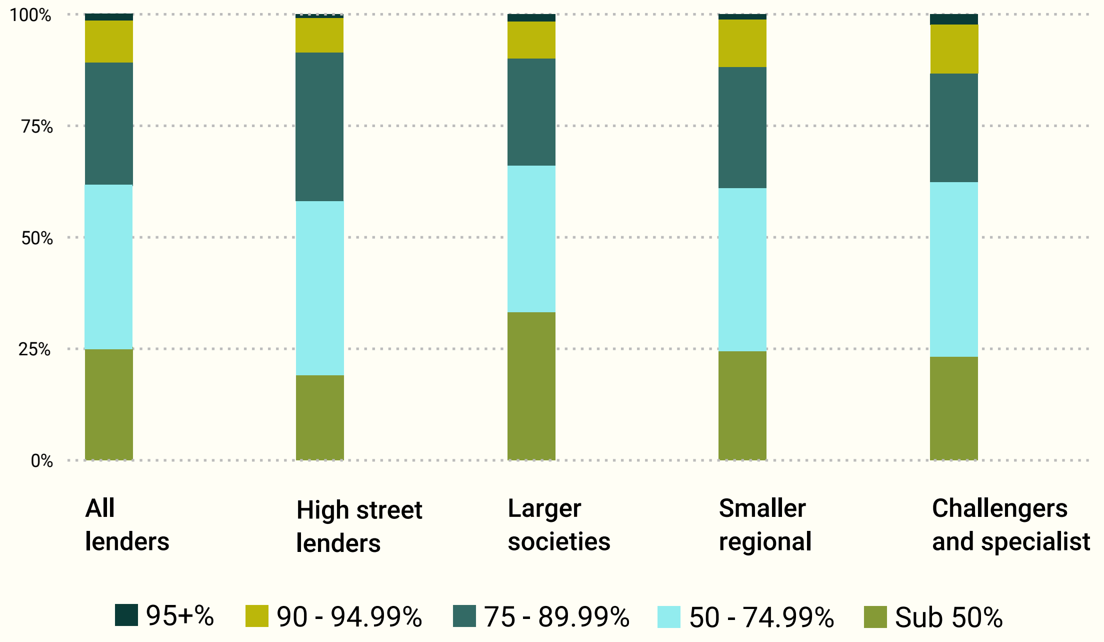
Lending mix

Our lenders are strongly represented across residential purchase, remortgage, and Buy-to-Let lending. This year saw Buy-to-Let lending across all lenders fall back to 26.3%, down 3.1% from the previous year—a resilient performance nonetheless, given the increased financing costs and regulatory and legal changes facing landlords.



LTV mix

Every year, we ask lenders about their split of LTV lending across product lines to understand which markets drive certain approaches to processing.



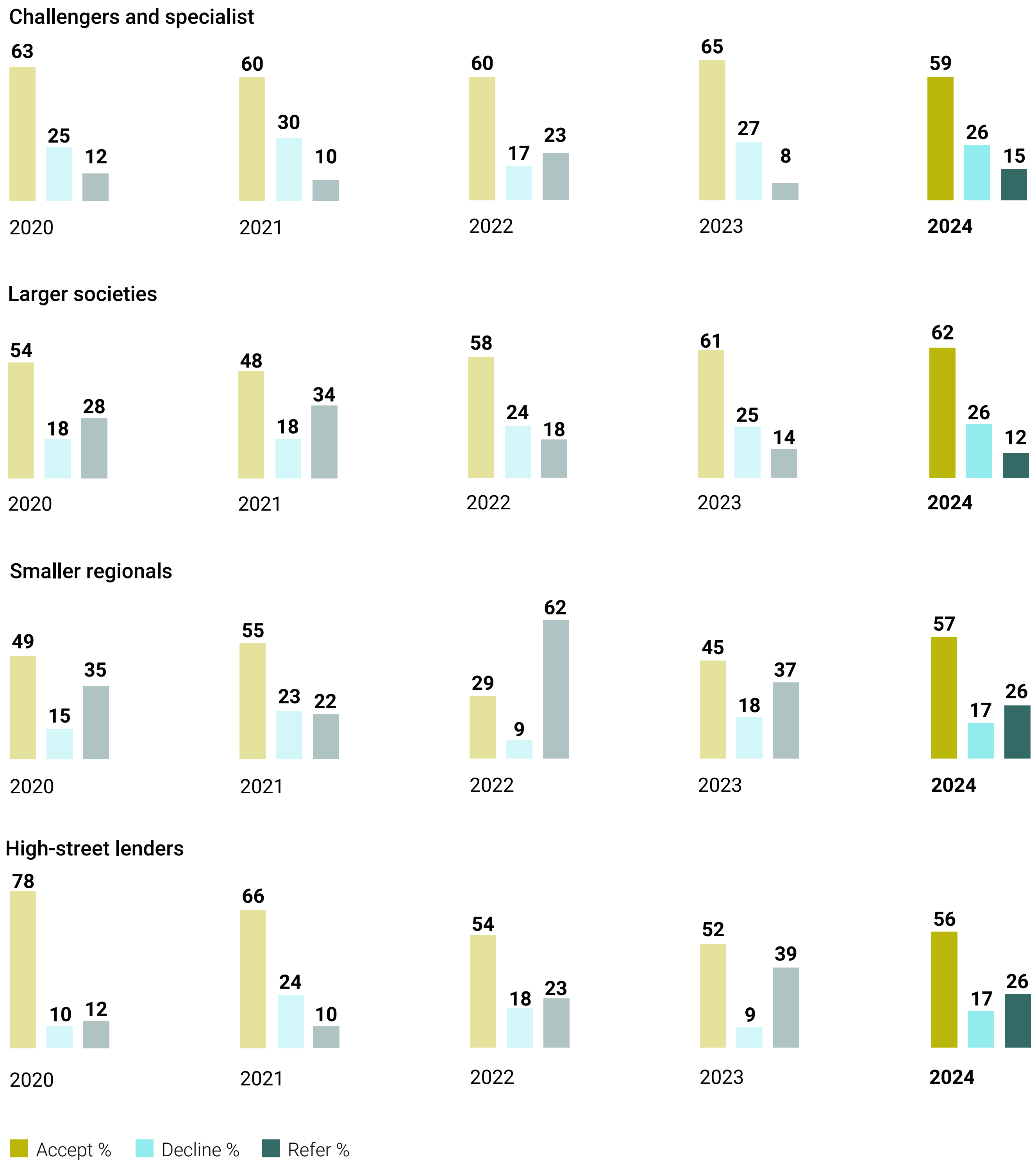
This year, on a percentage of lending basis, challengers and specialists and smaller regionals led the way in lending over 90%, with challengers and specialists excelling in 95% plus lending. This arguably reflects their role in offering manual underwriting in more complex and difficult areas of lending and perhaps also the increased demand for re-finance among a cohort that would have been exceptionally sensitive to affordability pressures. The high street lenders dominated the 50%-74% band and stood out again in the 75%-89%. Last year, challengers and specialists dominated these bandings, particularly the 75% to 89%. Challengers and specialists have stepped in to support higher LTV lending.

Larger societies were very strong in the sub-50% market and closely followed by challengers and specialists in the 95%+ market, suggesting a need for margin business but perhaps also reflecting their commitment to the first-time buyer market. Last year, sub-50% lending was dominated by smaller regionals.

From this year's responses, we can see that smaller regionals and challengers and specialists have moved up the LTV curve in response to competitive plays for lower LTV businesses, the growth arguably in higher LTV businesses, and the search for margins.

Decision to accept, decline or refer a Decision in Principle

Regarding processing decisions from their Decision in Principle (DiP), the four peer groups reported as follows for intermediary business.



Referrals diminish as confidence grows

Last year's data was taken after the mini-budget in September 2022, when rates were still moving quickly, and products were being hastily withdrawn and repriced. Affordability was not only the battleground; it was ongoing volatile territory.

Of particular note is the fall in the acceptance rate for challengers and specialists and the growth in referrals. Lenders in this peer group reported a fall in the quality of DiPs across the piece. Their experience reflects a more complex and distressed borrower environment.

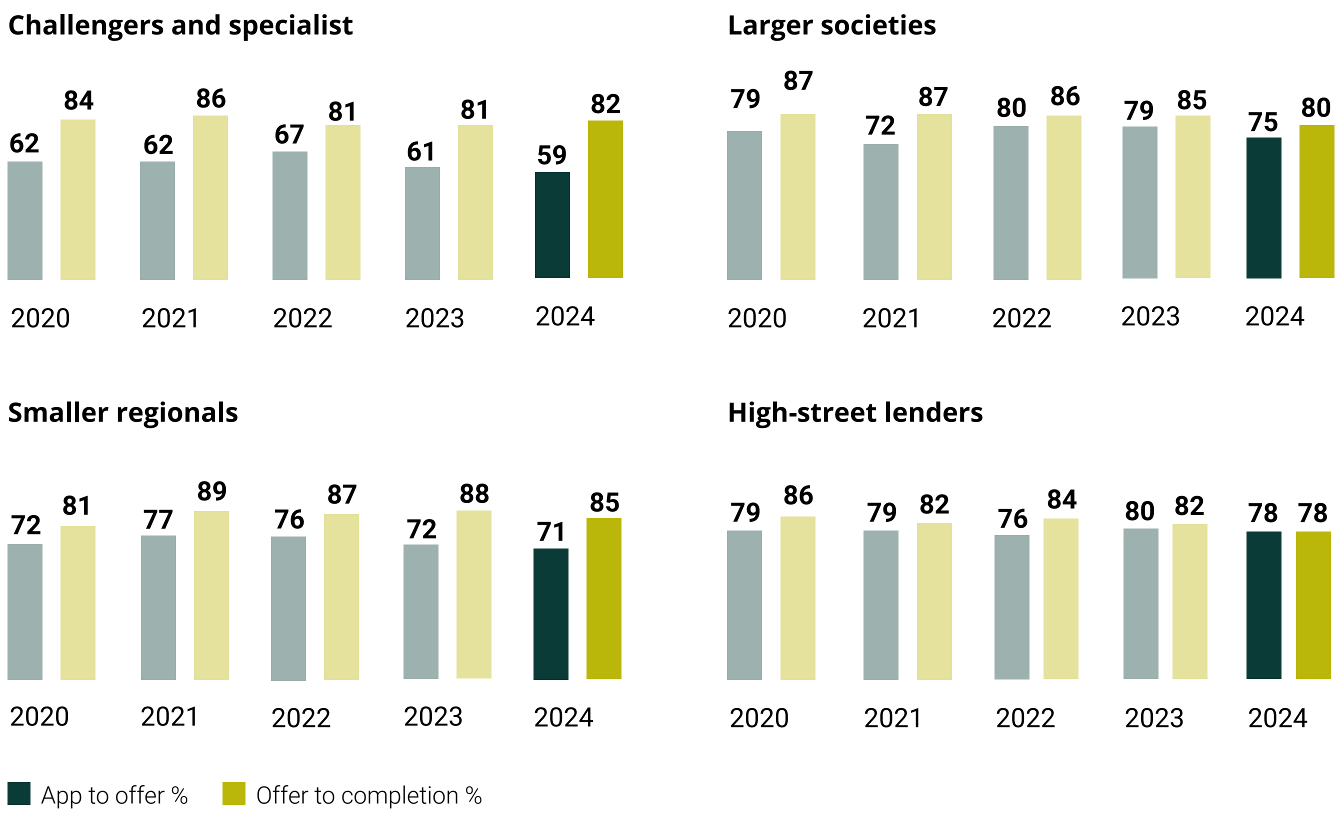
That dynamic is evident, too, in the High Street, where declines have grown as referrals have fallen—suggesting a more willing willingness to push back on cases perhaps now more suited to the specialist market and those markets that offer lower scale but also more labour-intensive manual underwriting.

Conversion Rates

When we looked at average conversion rates, lenders were clear that the volatile interest rate environment had impacted their ability to convert.

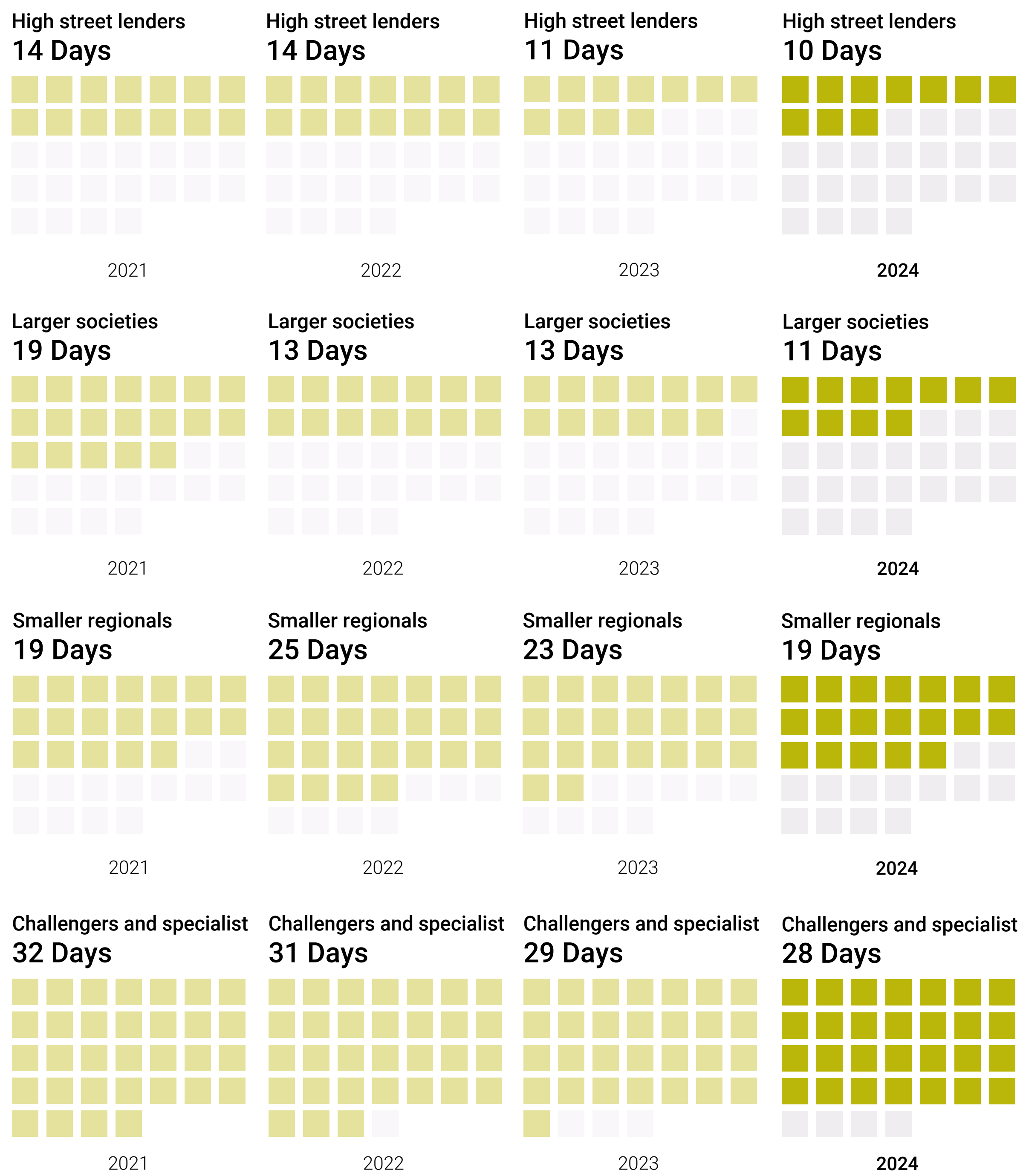
This issue had real commercial impacts for some as brokers swapped products post-application in the quest for the best pricing. Some reflected that the app-to-offer timescale must improve to deter product swapping in a volatile pricing environment.

One lender suggested that cancellation fees may need to be in place to protect funding costs, but many accepted this as a necessary evil. In the face of Consumer Duty rules, brokers must act in their borrowers' best interests to avoid 'foreseeable harm'. Many felt that while pricing remained relatively volatile, the market should expect this behaviour to continue. Whether it does in non-regulated businesses remains to be seen.



Notwithstanding the pressure of brokers swapping deals later in the process, offer and completion rates remain relatively stable. While all offer rates were lower than last year, the fall was not substantial. Completions, too, were down, with the exception of Challengers and Specialists.

This year we asked again, "On average, how long does it take to process applications to offer?"



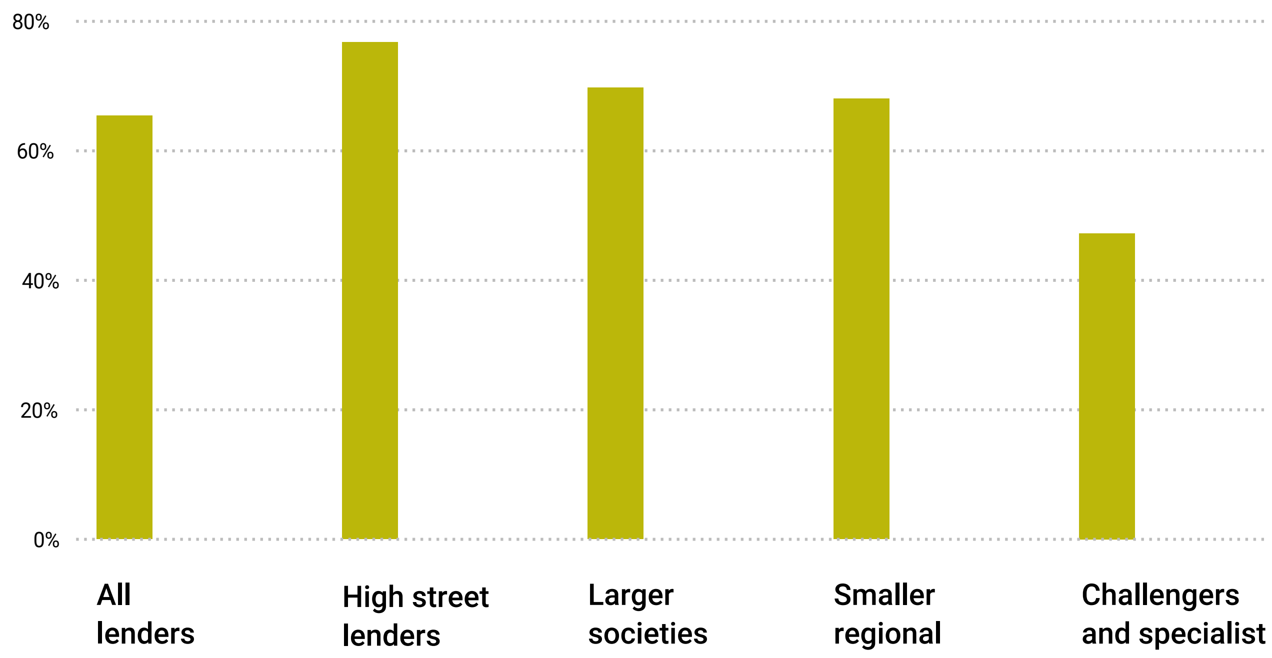
Last year, lenders highlighted underwriting and the impact of affordability on applications as the key reason for a more lengthy application-to-offer process. This year's data shows that all the peer groups had made inroads into speeding up their Application to Offer process, whether that was about greater confidence in decision making or a reflection of the need to keep business on the books once the Application was in. Equally, the reduced lending volumes over 2023 may well have helped conveyancers and valuers deliver more efficiently. The most notable improvement was in the processing time of Smaller Regionals, returning to levels last seen in 2021.

Retention rates

The average retention rate of 62% improved incrementally to 66%. High Street Lenders led the way with an average of 77%.

Challengers and Specialists significantly rose from 36% last year to 47% this year. For some newer players, this reflected improvements in processes over the last 12 months and, more generally, better strategies for coping with maturing product cohorts.

Average retention rate



02

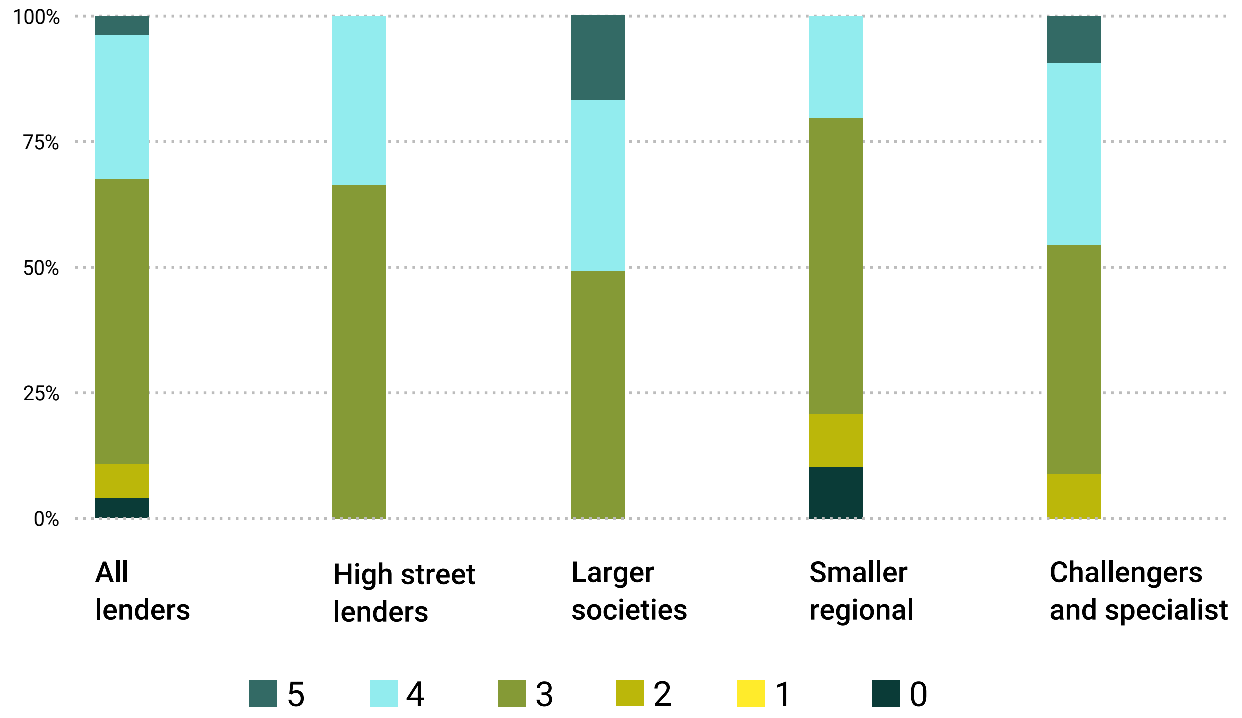
The focus for improvements has changed

Pre-DiP and Affordability

We asked lenders about the level of automation and technological integration in their initial interaction with intermediaries and borrowers through affordability calculators and scored lenders' satisfaction with their process.

This year, 94% of lenders scored themselves with a 3 or 4 score (compared to 78% last year), which, in our conversations, reflected a belief that the tools were largely fit for purpose and reflected broker feedback.

On a scale of 0-5, how happy are you with your current levels of automation?



Satisfaction scores: 5 is the most satisfied and 0 the least satisfied.

There has been little investment in technology or third-party data links for calculators, with many accepting that screen scraping was as far as any calculator integration went and was likely to in the near to middle future. Lenders almost universally use a blend of client-supplied data and ONS data for affordability calculations. How these two data sources interact exposes some differences as lenders decide on one or the other depending on the validity of client-supplied data. Many still review their ONS data usage quarterly to check on affordability constraints. Still, overall, there was a quantum leap in confidence around affordability calculators compared to last year, as reflected in the scores.

Calculators have evolved in many cases to reflect changes in affordability calculations (five-year fixed rates drove a lot of this work) and changes in stress rates or income multiples for particular markets like new builds. Very few calculators suggest alternative products in the event of an affordability failure.

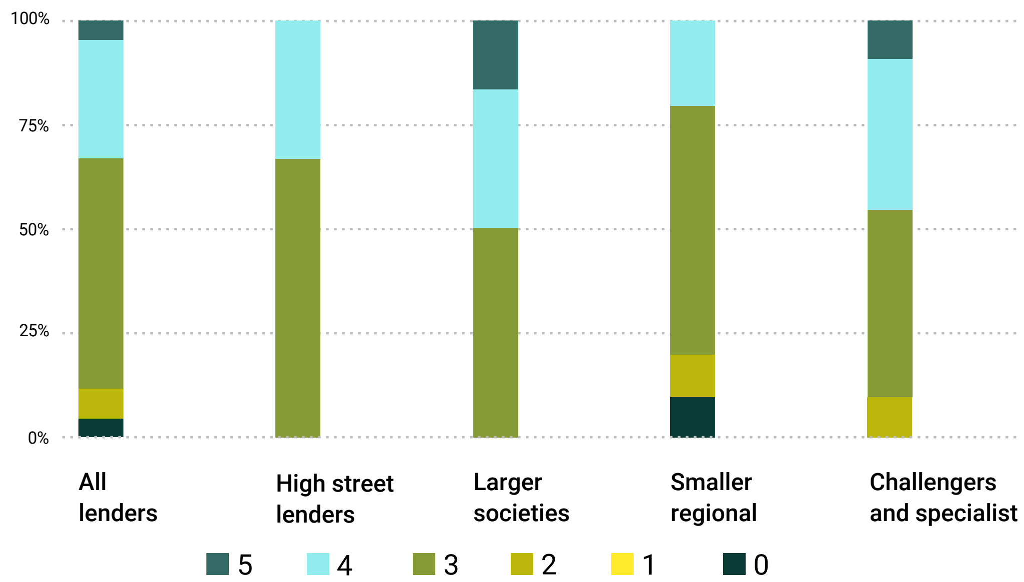
As with the DiP process, some lenders observed that regular users of their calculators and DiPs were invariably more positive about that technology than infrequent users. There were very few who highlighted this part of the process as a point of focus for improvement over the next 12 months.

Where upgrades to calculators and DiPs were mentioned, it was as part of a far bigger re-invention of the technology platform.

Decision in Principle

We asked lenders about the level of automation and technological integration in their Decision in Principle process and assessed lenders' satisfaction with it

On a scale of 0-5, how happy are you with your current levels of automation?



Satisfaction scores: 5 is the most satisfied and 0 the least satisfied.

In 2023, the overall satisfaction score across all lenders registered 75% scoring between a 3 and a 4. This year saw this score rise to 82%. Indeed, improvements were visible, particularly among Small Regionals. Last year, 7% had scored their DiP with a 0; this year, that answer was 10% and 70% of that peer group scored their DiP process with a 3 or 4.

While there was no movement among High Street Lenders (100% again scoring their DiP within a score of 3 to 4), Challengers and Specialists saw an increase from 73% to 91% registering a satisfaction score of 3 or 4.

Larger Societies reported scores of 83% across the 3 and 4 bands in 2023, with 17% scoring 5. This year saw no change in the Larger societies satisfaction scores for the DiP stage.

Overall, our conversations reflected the work started last year regarding addressing key questions, such as reducing the volume of questions asked at DiP stage and the development of other data sources. Only a handful of lenders still run a hard footprint search at the DiP stage, and at the other end of the scale, a growing number are trialling AVMs at DiP. While implementing EPC data at the DiP stage remains an aspiration for 99% of lenders, the journey to net zero will mean that it remains on most roadmaps – particularly if it becomes integral to origination strategy and product pricing in the longer term. Some lenders have also moved ID&V forward from their application process to the DiP.

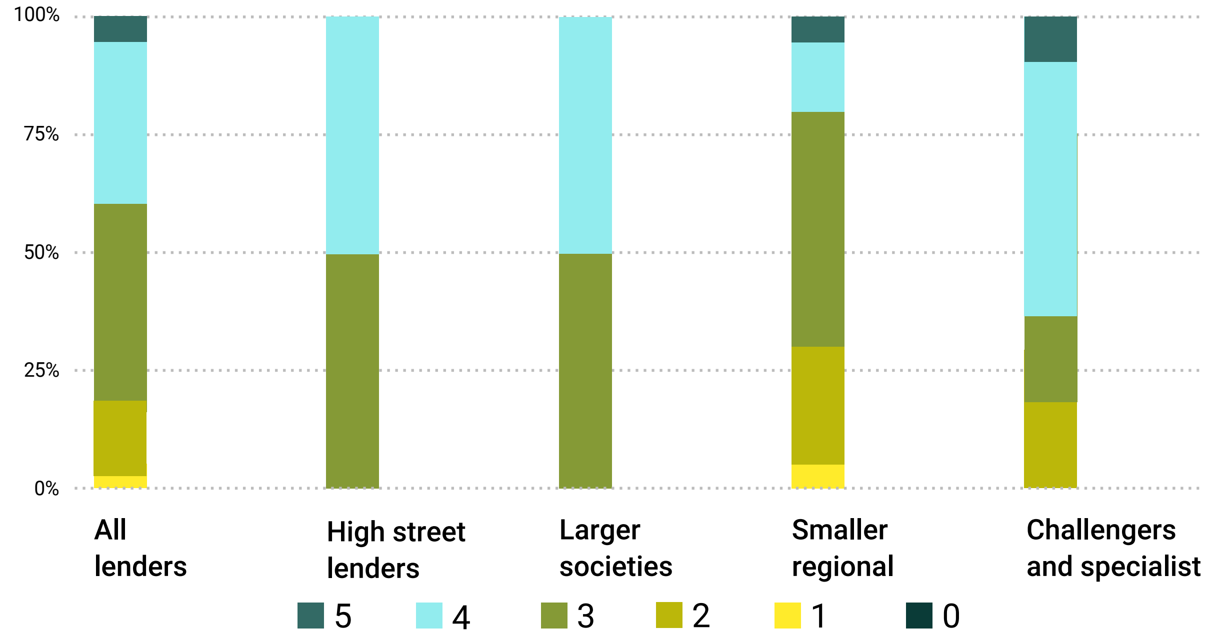
The key performance indicator for the DiP remains to provide the earliest highest possible level of certainty in the decision given to the broker and borrower.

Full Mortgage Application

Lenders have applied learnings, but there is still much to do

We asked lenders about the level of automation and technological integration in their full mortgage application process and their satisfaction with it.

On a scale of 0-5, how happy are you with your current levels of automation?



Satisfaction scores: 5 is the most satisfied and 0 the least satisfied.

Last year, 75% of lenders scored their application process between 3 and 4, and this year, there was a marginal improvement to 77% scoring similarly over the two bandings. However, at an individual peer group level, there were some interesting changes.

The results of High Street Lenders and Larger Societies remained static year on year with a 50/50 split of satisfaction sentiment across scores of 3 and 4.

Smaller Regionals registered a shift in scoring. Last year, 7% scored their application process with a 1, but this year, this had improved to 5%.

Last year, 18% of Challengers and Specialists registered a score of 5, which slipped to 9% in 2024's results.

Toward the end of our survey, we asked lenders where they would invest if they could, and the scores here reflect the overwhelming number of responses in the FMA and Offer parts of the process.

"We need to keep data capture light…"

Almost all lenders stated in conversation that efficiencies in underwriting would be welcome. Too many underwriters still have to look too closely at cases that should go through automatically in many cases. Importantly, lenders are keen to reduce the volume of document chasing (or packaging) that underwriters have to undertake. But more than that, many responders reflected that relying less on client-supplied information and more on other data sources would help slim down the process and allow underwriting staff to concentrate on the cases that really needed their attention.

Technology changes were reported in two areas. The first was in the scaling of data sourcing. There was an uplift in the number of lenders using AVMs for new business, but there was more uplift in the volume of AVMs used within lenders where the facility was already in use. The second was using external data sources to replace or validate 'client-supplied' data.

Confidence in data is key in these decisions, as is confidence in the suppliers of data solutions. This is not only in the commercial sense of correct, timely, complete information but also from an interoperability point of view. We heard very little with regard to the establishment of new commercial providers for data and technology services. However, we did hear many lenders refer to current providers, in whom they have already significant trust, providing new data sources.

One new noticeable development reported this year was the number of lenders now using more than one credit referencing agency in their process to improve performance and 'fill gaps' where necessary.

Little to no progress had been made in 'Open Banking'. As mentioned, many lenders are using current data providers to supply data sources like income verification. This supports a view long expressed by many that they do not need more data to create more work but want it to streamline an already manual process. Lenders are keen to see data that validates a view – not to create more workload. The value that Open Banking in its broadest sense, can provide is not perceived by many lenders. Open Banking, in whatever guise it ultimately manifests, was more positively discussed than in previous years but almost entirely from the point of view of validating income decisions and being employed in a slimmed-down version to deliver efficiencies – not to raise more questions.

Offers

Offers see renewed interest

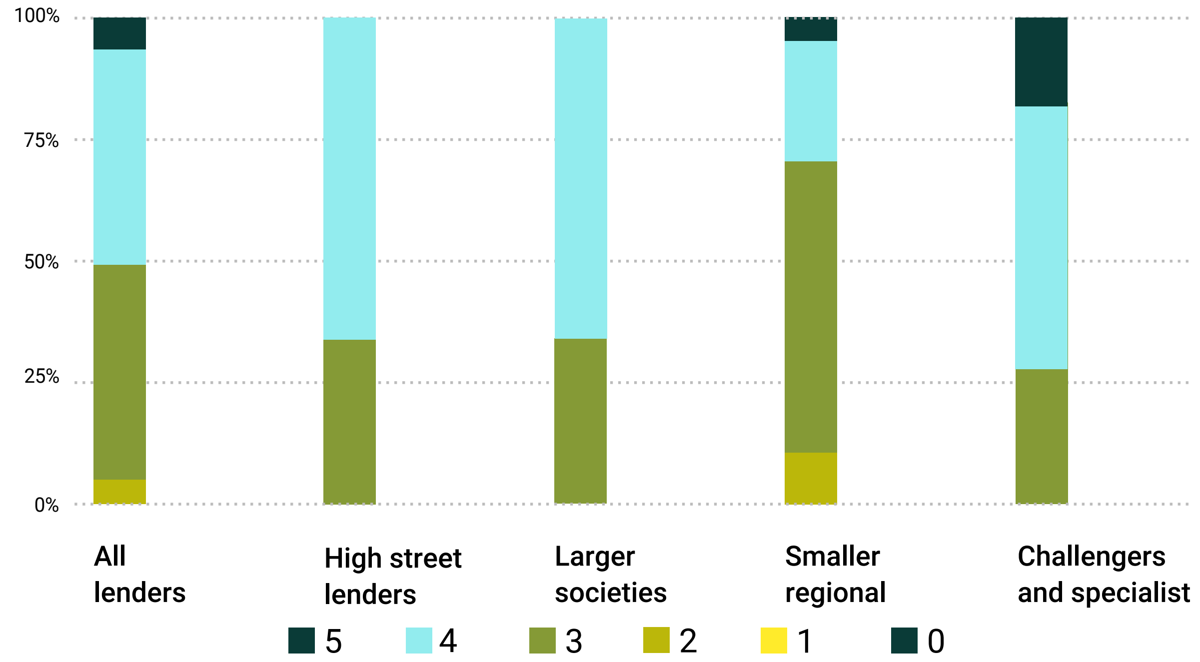
Last year, over half of all the lenders we asked scored their process with a 4, but this year, this has slipped to 44%. However, when we look at the combined score for 3 or 4 last year (84%), we can see that this year, that score has improved to 88%.

Within that headline are some interesting movements that reflect the time, energy, and money invested in the offer process.

Last year, 17% of Larger Societies responded with a score of 2 for the offer process, but this year, no scores registered under 3. The percentage of Smaller Regionals recording a score of 2 in 2023 also fell from 14% to 10%.

All other peer groups scored 3 or above.

On a scale of 0-5, how happy are you with your current levels of automation?



Satisfaction scores: 5 is the most satisfied and 0 the least satisfied.

This year's obvious steps forward again included the almost total abandonment of wet signatures (excluding for direct debits), secure electronic delivery of offers, automated special conditions, and a noticeable uptick in the number of lenders using electronic Certificate of Titles in their offer process.

Many lenders this year, in a change of focus, had spent time improving systems and processes for this part of the mortgage operation. It remains a work in progress. When we asked lenders which part of the mortgage process they would improve first if possible, offers, along with the underwriting part of the FMA, were top of the pain points – partly because of the conveyancing issues. e-COTs are in wider use and still remain the gold standard among advocates in injecting efficiencies into the offer process.

Completion

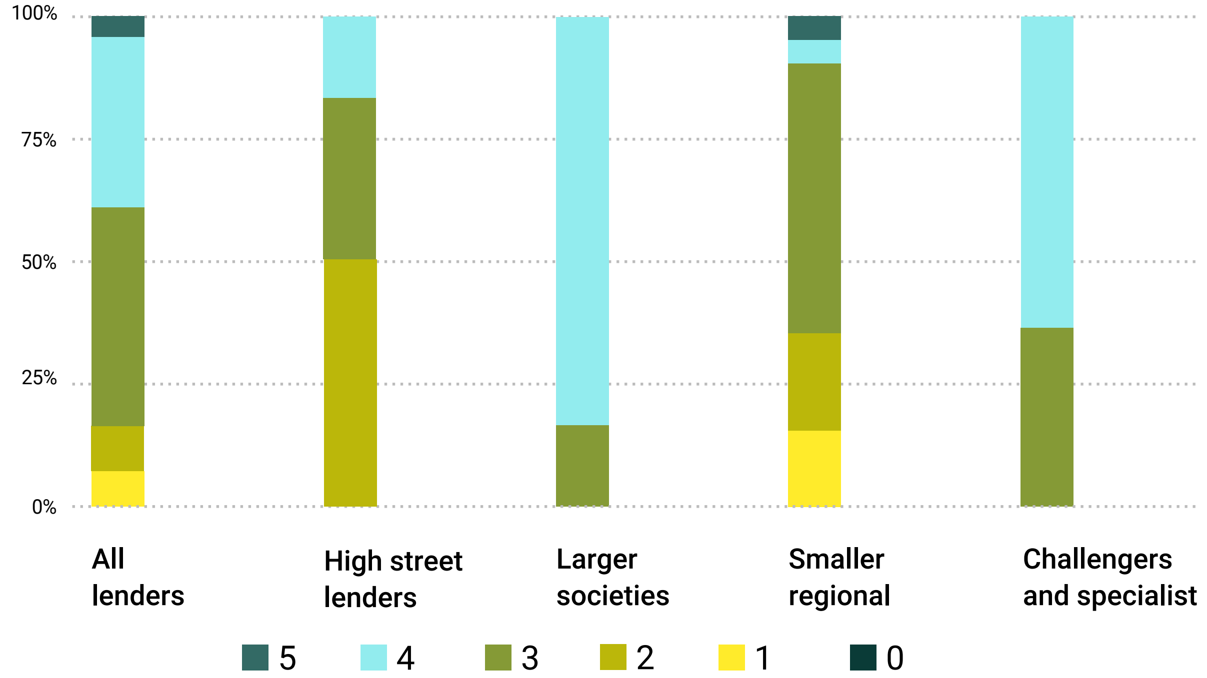
Last and still least - the full completion picture

We asked lenders about the level of automation and technological integration in their completion process and their satisfaction with it.

Last year, 53% across all groups scored a 4, with Larger Societies leading the way, but this was not repeated. Only 35% across all groups scored a 4.

Smaller regionals registered a growing dissatisfaction with their performance in completions this year with 35% scoring a 2 or less compared to 28% last year.

On a scale of 0-5, how happy are you with the performance of your current levels of automation?



Satisfaction scores: 5 is the most satisfied and 0 the least satisfied.

Completions remain the Cinderella part of the mortgage process, if only due to the peaks and troughs in completions fluctuating according to purchase market demand and stimulus. As was last year, the consensus is that what is in place works well enough for all concerned and that 'in extremis' lenders are happy to "throw bodies at it" until the normal order of things is restored. Batch runs for funds release, and the payment of proc fees remain very manual processes for many lenders, and there remain multiple manual checks on payments. Some lenders manually complete cases onto the core banking system, as opposed to utilising contemporary API technology. These are unsurprisingly, though not exclusively, lenders who are not operating at scale and are very often saddled with legacy processes and systems.

Product launches, withdrawals and criteria changes come in for scrutiny

This year, we again asked a question that sought to understand lenders' views on their product launches, withdrawals, and criteria changes.

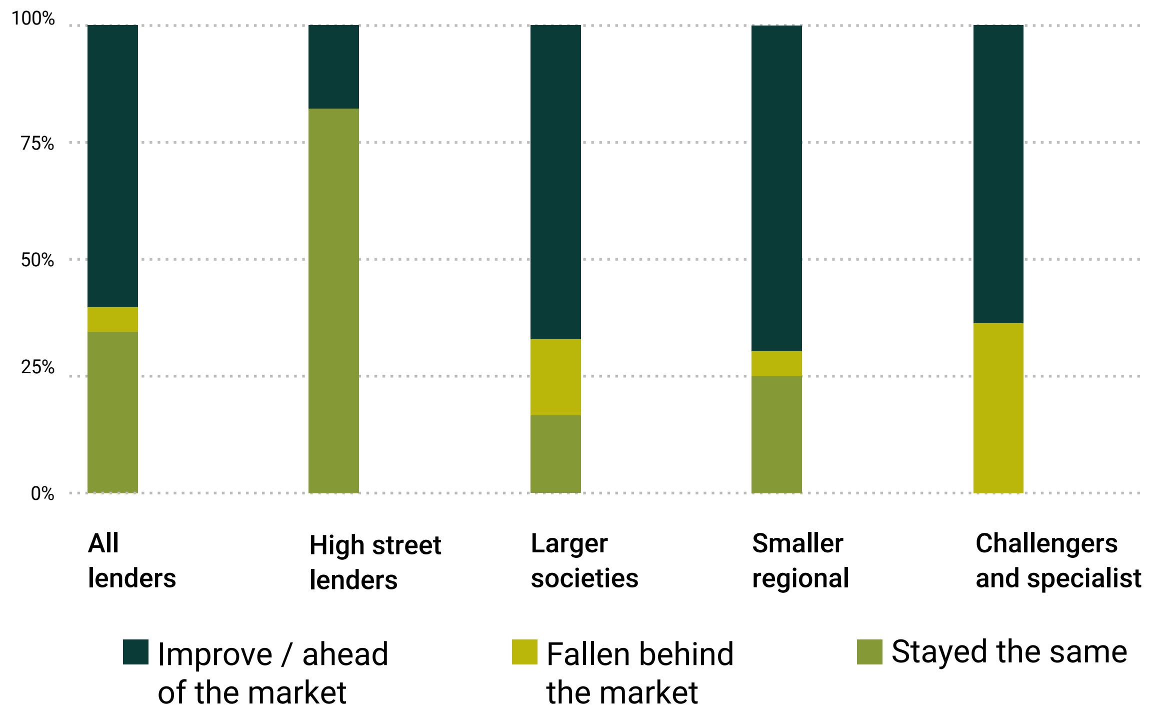
However, rather than scoring the processes, we wanted to know if they had made improvements since the change in operating environment spawned by the mini-budget of September 2022 and where they saw those changes in relation to their own experience and the broader markets.

In terms of overall sentiment with regard to the success of product launches, 61% believed their processes had improved. From our survey last year, the stimulus given to lenders to improve these procedures was significant. Having the wrong products in the market at the wrong time not only damaged margins but the consequent inundation of applications also damaged service levels, hampering attempts to correct any pricing damage with new launches.

These improvements were not all technology-based. Re-engineering sign-off procedures, creating new departments, reassigning responsibilities, and hiring people all figured in the conversation about why product launches were in a much better place.

83% of the High Street peer group reported that their processes have remained the same, and 5% of smaller regionals and 17% of larger regionals believed they had fallen behind.

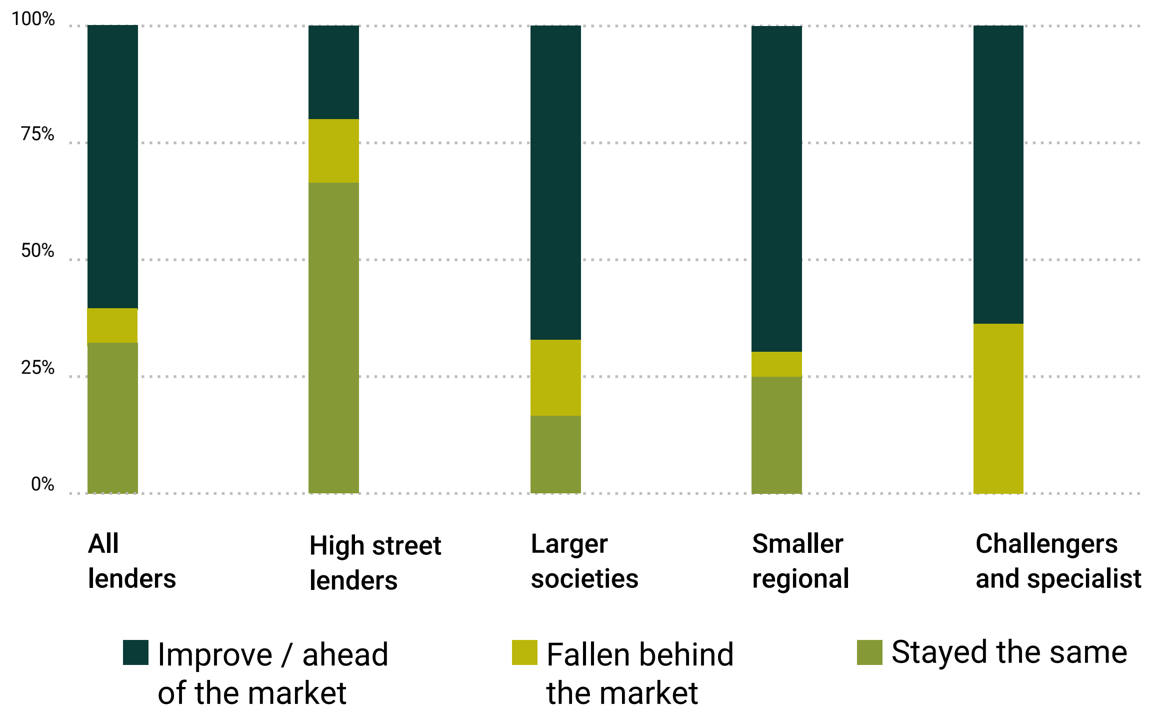
Over the last 12 months how do you believe your processes for prouct launches have progressed?



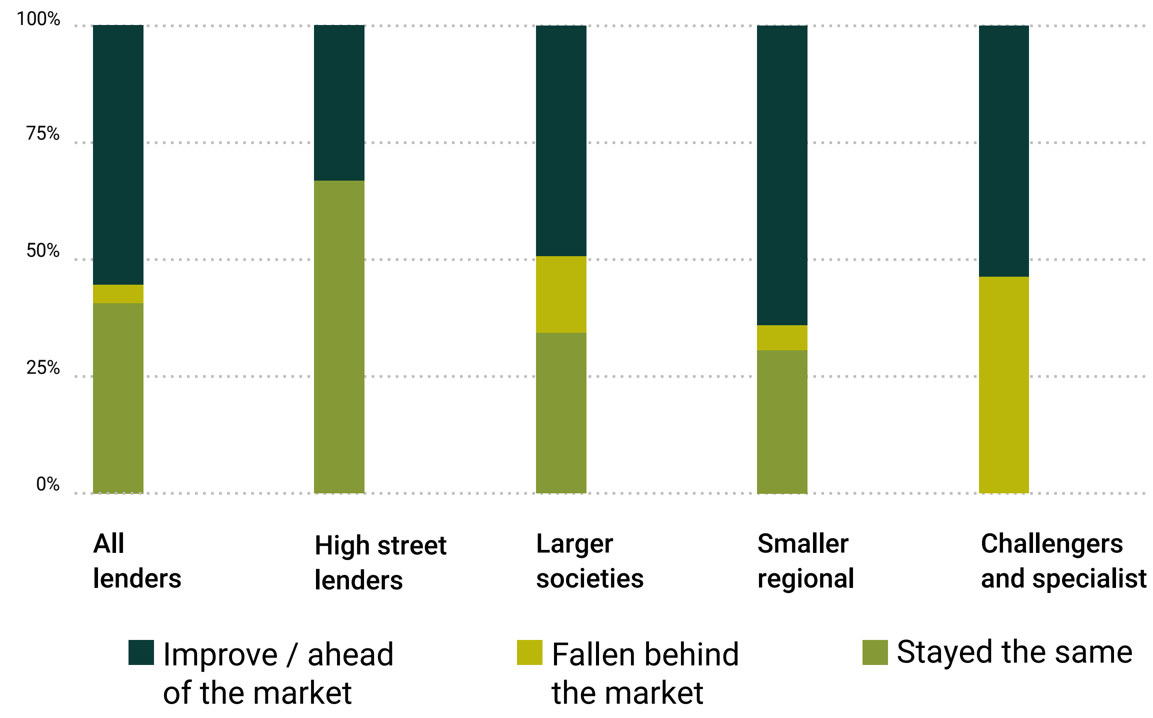
In terms of product withdrawals, the major consideration among all intermediary lenders was being fair to distributors. 'Fair,' of course, looked different to individual lenders, but the broader point was that while instant withdrawals were very possible, they were the option of last resort. The time allowed to brokers by most simply reflected their market.

61% across the piece reflected that product withdrawal processes had improved with only 7% reporting these had fallen behind – largely High Street Lenders and Larger Regionals.

Over the last 12 months how do you believe your processes for product withdrawals have progressed?



Over the last 12 months how do you believe your processes for criteria and policy changes have progressed?



In terms of improving product criteria and policy changes, 56% believed they had made improvements in this area. Where there were fears that lenders had fallen behind, these were in the Larger Societies and Smaller Regionals peers.

03

Where next for mortgage technology, data and lending?

The path of least resistance

This year, our conversations revealed just how many lenders are currently or about to re-platform their operations. We alluded to this in previous reports and reflect the realisation that legacy technology cannot deliver what lenders need today.

Time and again, when we inquired about changes in the last 12 months to various parts of the process, the answer was that little had changed because bigger, more sweeping changes were taking place in the background. Many of these programmes will be delivered in the next two years, but they are for now an explanation for why some lenders appear to have 'stood still' in terms of technology investment over the last two years.

In terms of data and interoperability, lenders remain keen to use technology and data to improve efficiencies, but their approach has changed.

From an interoperability point of view, while the vast majority view alternative data sources as being at the top of the list to improve elements of the mortgage processing experience, such as affordability data or payroll services, it is clear that lenders are very reluctant to push ahead with unknown providers. Incumbents hold the keys because they are perceived to carry less risk. Whether this is true or not (as we have seen with Microsoft and CrowdStrike) is not the issue. Current providers offer the path of least resistance.

Housing and a new government

Do you expect housing to be an election issue, and will a post-election government have a positive, negative, or zero impact on housing supply and mortgage affordability? What do you want to see?

"This is very likely to be the same meat with different gravy."

At the time of the survey (conducted in May and June), we asked responders how they believed an incoming government of any colour would impact the housing market. While manifestoes and policy leaks were already available outlining future aspirations, most responders expected little change. Many thought that now, as with previous administrations, much of what has been promised in terms of planning reform will fall short of providing the houses required to address the lack of supply. Ultimately, everyone expressed concerns about the delivery of new plans, and few appeared to be using the Mortgage Guarantee Scheme as it was generally considered to be commercially not worth it.

"It would be helpful if we had a housing minister in post for more than six months"

Nevertheless, schemes for supporting home ownership were on many people's wishlists. These ranged from reinstating Help-to-Buy to extending the stamp duty cut next March, removing stamp duty for downsizers, or offering further first-time buyer support. Some were keen to point out the requirement for a broader plan across all tenures and cross-party rather than just a focus on new builds and more help for markets such as shared ownership.

"We need a scheme that is serious about supporting levelling up."

Specialist lenders were keen to see the plight of landlords addressed but few held out any hope of change here.

Several lenders pointed to an interest rate cut and perhaps a change to current LTI limits as promising more decisive action more quickly, but again, they were not hopeful of either imminently.

Consumer Duty

How has this gone so far? What have you been doing and is there anything that remains outstanding regarding cultural or process change?

We were keen to understand how consumer duty had impacted the operational nature of lenders' business.

"The Dear CEO letter focused minds"

We first enquired about lessons learned and observations around the first implementation of consumer duty on originations. Many lenders, particularly, though not exclusively, in the mutual sector, felt it was an extension of current practices and culture. However, even there, some lenders agreed that processes had been sharpened up. Generally, for most lenders, consumer duty was invariably about getting current practices into shape.

However, no lenders claimed to have sailed through the implementation. Most lenders reported that gathering the MI was the greatest challenge of implementing Consumer Duty. Some did feel that they had initially possibly underestimated the impact and requirements of implementation on the business – this was particularly the case for smaller lenders.

Some specialists in Buy-to-Let, although not technically under the same regulatory auspices as residential lenders, had implemented the practices where, for example, parent companies were retail banks.

Many of the responders spoke about improved regularity of communications with borrowers to inform them of other options, but several also pointed out that for whatever reason, some borrowers resolutely resisted and preferred to remain on current products. This was a consensus view, but of particular note was the comment from one lender that it was mulling the idea of automatically lowering borrowers' rates when applicable.

Vulnerability

When we asked about distribution challenges, the conversation invariably turned to fees and issues around declarations of vulnerability.

"There's a lot to unpack around vulnerability"

With regards to vulnerability, some lenders highlighted the complexity around different distributors having different models. This one issue highlights the complexity of the new rules within the current lines of delineation between product provision and advice. Every lender to whom we spoke referenced consumer duty work as auditing current practices - in effect, evidencing what currently happens is up to scratch. No one as yet has raised the prospect that in certain elements, hand-off points may need to change or, indeed may become blurred in the future. Vulnerability, however is one area in which that may happen. While all seemed comfortable with progress to date, one lender told us that now was the time to step back, assess the effectiveness of what had been done and develop a plan for further change.

Interestingly, several building societies pointed out that fair value assessments had proven harder in the retail deposit market, with ideas of fair value being derived from peer group behaviour.

With regard to the compliance of closed books with consumer duty rules, lenders felt again that, for the most part, legacy SVR pricing had already been addressed. Still, they acknowledged work needed to be done with regard to the timeliness of existing property and credit data. One lender reported that borrowers were already entitled to switch to new products even if they were in arrears. As mentioned, only one lender is considering automatically lowering borrowers' rates.

Basel 3.1

As an addendum to the application of Consumer Duty rules to back and closed books this year and the subsequent assessment of credit and asset data, we asked about the likely impact of Basel 3.1

While the rules are not finalised, a few lenders alluded to their expectations of the capital changes. 'Holiday Lets' was already a market some had abandoned in the expectation that the revised risk weighting of the market as a commercial loan would prove too much for the balance sheet and profitability.

One lender was upbeat about the changes, expecting that they would increase competition in the market for vanilla and specialist lending as lenders recalibrated their approaches. The new rules would arguably see more High Street Lenders enter specialist markets and more specialists enabled to compete for vanilla business.

Green

Do you offer incentives for green home purchases or retrofit/improvement loans? What issues do you perceive in delivering this? Do you collect EPC ratings and other property-relevant information?

> *"Our experience is that it's all push and no pull"*

Only a couple of years ago, the Environmental element of ESG sat at the heart of many lenders' plans. As of today, that impetus has slowed. The infamous mini-budget and its subsequent impact on pricing and standards of living has meant consumers have little appetite for investing thousands of pounds in retrofitting property. Many lenders highlighted the broader lack of consumer appetite. The cost-of-living crisis has played a significant part in hastening the dwindling interest from borrowers. Furthermore, a few lenders raised the issue of how important it is to not greenwash.

With the exception of a couple of lenders who had released new products since our previous survey, the focus has been entirely on the scope 3 emissions reporting of back books. Most lenders were keen, on the whole, to point out that this would not mean incentivising better EPC-rated properties to address the average EPC rating of their books, but some are offering better deals for new builds with A or B ratings.

Regarding originating business, lenders believe the government needs to play a more significant role. As one lender explained, a cashback of £500 is of little consequence if you face a retrofit bill of £5000. Lenders are expecting the government to incentivise home-owners through fiscal sticks and carrots ultimately.

> *"Lenders are a conduit – there is a limit to what they can do."*

In addition, there are unknown unknowns about some of the building regulations that are being put in place to enhance energy performance. Air-tightness may be energy efficient but its impact on mental health is unknown. The law of unintended consequences looms large, and while lenders are happy to sign-post possible options for borrowers, they remain reluctant to prescribe action. Previous attempts by the government to influence home-owner behaviour live long in the memory as some remember the government's attempts to insulate wooden frame houses with spray foam insulation, which resulted in catastrophe for some homeowners.

In short, a complex topic requires nuance, and that is expensive. With margins under pressure, every lender seemed sceptical that whatever they could afford to do would spur homeowners to 'do more'. However, there was some consensus around the value of sign-posting borrowers to better behaviours.

On a brighter note, however, more progress was reported among organisations offering green savings schemes, which seemed to have been welcomed by certain customer cohorts.

AI

What do you understand this to mean in the context of mortgage processing? Do you believe AI constitutes a threat, an opportunity, or both, and upon whom and where might it have the most impact?

> *"We're a fast follower."*

> *"We have a watching brief – we need to understand when and where it can add value safely."*

> *"We should not get caught up in the hype"*

Most lenders view AI as machine learning and, at present, consider the impact of AI entirely from an organisational impact view. Most lenders viewed AI as machine learning with varying impacts on their operations. For the vast majority, it was seen as complementing current human roles in providing services. Indeed, for building societies, adoption while retaining that personal touch was a key point. The more niche a lender's business is, the more the appetite for AI solutions is considered. Much of the mutual market relies on manual underwriting and experience to get deals over the line and all were keen not to compromise that.

For many, efficiencies and consistency were key to any adoption. Some had already embedded features such as chatbot solutions and were mulling 'execution only plus' journeys while the majority were keeping a watching brief. One or two reported running a sandbox environment to trial AI technology.

Where machine learning was thought to offer possible breakthroughs is in the area of product modelling. Examining vast datasets and understanding borrower performance is one area highlighted as ripe for innovation with the prospect of moving from LTV pricing to individual pricing mentioned by one lender. Many responders highlighted that any area of data capture and data assessment was considered by many to be an obvious starting point for AI solutions – especially where big legacy systems are holding lenders back.

Of particular interest was lenders' approach to educating the workforce on employing solutions. One lender was already encouraging large numbers of staff to take AI qualifications. Others, though saw the more digital interactions of younger generations in the workforce as a hint of what might yet come – citing an interest in AI BDMs, among other possibilities.

Finally, where lenders have not begun assessing AI is how it may impact their borrowers. For some, that is a reflection of their current borrower type, but it was interesting that no one highlighted concerns about how AI might impact the broader job market and borrower prospects.

Cyber security

Cyber security and digital fraud threats grow year on year. Do you see problems with integrating systems and digitalising your business?

"Risk versus reward."

Perhaps unsurprisingly, lenders' views of the risk presented by cybercrime and digital fraud varied according to the size of their perceived potential exposure. In many cases, smaller lenders pointed to their investment in InfoSec posts and the building of specific departments to address threats. For larger lenders, provisions and huge infrastructure investments formed a large part of their response.

"The debate has to be service versus safety."

For the High-Street peer group, there was total consensus about the need for cyber security and its impact on their willingness to integrate and exchange with third-party systems. The risk and reward equation of external technical infrastructure or data relationships is, for many, at the heart of any decision to move forward with external partners. The prospect of huge data leaks does worry lenders and sizeable provisions are often in place for such an event. Where lenders were considering making new data purchases (for example Auto Income Verification) or developing elements of open banking functionality, it was through big established players already providing other services.

"We have to manage and move on."

The consensus view was that cyber security and fraud would not deter lenders from doing the right thing commercially, but they are already a significant hurdle for those coming to market with new products.

Middleware

Why is broker adoption of market connectivity software slow? Is it an important capability for lenders to support?

"It's a solution for a problem no one wants to solve"

We wanted to understand since the availability of middleware connectivity solutions is fairly widespread, why so few lenders and brokers have adopted solutions that offer enhanced speed of application.
For many lenders, this was about opportunity cost. If the market embraced this kind of solution, then so would they. However, that momentum is missing. The top six lenders have huge reservations about delivering new business through these systems. If they can achieve the volumes they need as they are, then why do they need these solutions? Is the risk worth the reward? For others, too, these solutions may damage their competitive advantage. This was particularly the case for specialists.

"Burned fingers from the past have taught us all to be wary."

For brokers too, it was thought this was not a service they would want to pay for. Additionally, many of the administrators that key on the applications also fulfil other vital roles in the business. In effect, it does not save employment costs. Equally there were feelings that brokers, particularly in market stress, want to know they have secured the product from the lender. That update times on sourcing systems are too often not 'real-time' further undermines the idea of real-time interoperability. Finally, broker firms are too small in many instances to take on board more technology with all of the other requirements being made of them at the moment.

If money was no object

If we gave you £1m, what part of the process would you spend it on first and why?

It's not often that our questions miss the mark, but we quickly had to increase this amount to £5m.

We asked this question to understand lenders' priorities for the immediate future in terms of employing more technology to improve the mortgage journey.

Almost without exception, the answers lay in developing more support for underwriters and improving internal system performance with external data. While the digital journey for brokers was included in this, it was less about front-facing systems and much more about improvements behind the scenes, improving the accuracy, consistency and speed of decisions. Underwriting and the offer process were at the top of many lists not only because they were 'easy wins' but because they offered the most efficient means of delivering offers.

04 Conclusion

The focus for lenders is on getting their houses in order

This year's regulatory challenges, in addition to the market challenges, arguably both emanating from political decisions, have meant lenders have had to prioritise.

The current market and likely future regulatory changes make clear that new operating models and systems will be a must-have if lenders are to not only thrive but survive over the coming years. Agility is essential when so much change is in sight. Our political aspirations to build more housing, our regulatory desire to reduce risk, our economic battle to control inflation, the social dynamic of our aging population, and the impact of technology on borrowers, banking and funding means the challenges will likely grow. Knowing how your peer group is coping too is arguably more difficult when all are available through a web browser if not physically present on the high-street.

The growth of digital opportunity comes with other challenges and expectations. Lenders need to understand not only who they contract to deliver a job but also who else is involved in that delivery. Who oversees the subcontractors' subcontractors? CrowdStrike showed just how critical this may become in due course and explains why so many larger lenders and small ones have concerns about increasing their exposures to third-party systems.

So, while brokers and consumers will expect and demand a more efficient and better digital experience, concerns about cyber security will mean this delivery will be incremental. As we have seen in this report, the focus is on getting lenders' houses in order—it's change that is necessary but also can be rigorously controlled.

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