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Unsustainable Home Ownership and Over-indebtedness: the experience in Britain and its relevance to other European countries

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Introduction

This paper discusses some recent developments with respect to home ownership in Britain and suggests that they have potential relevance for understanding the likely direction of development in other European countries.

The paper is organised in three sections. First, it considers the expansion of home ownership in Britain and identifies the pre-requisites of sustainable or non-problematic owner occupation. Second, it identifies a set of developments which have resulted in the fragmentation and unravelling of the relationships and prerequisites that have traditionally sustained home ownership. As a result there has been a significant increase in unsustainable home ownership in the form of a growth in the incidence of over-indebted households and households who lose their property through the judicial process. At the end of 1998, 361 000 households were in default with their mortgage payments. During 1998, 33 840 households lost their homes due to an inability to pay. As will be discussed later, these figures are much higher than was the case in the early 1980s. The recent trend in the incidence of unsustainable home ownership in Britain will be considered along with the characteristics of those who are over-indebted and some comments made on the likely future direction of developments. In the third and final section the paper will consider the relevance of the UK experience for other European countries.

1. The expansion of home ownership in the UK

Currently 68 per cent of households in Britain (16 million) own their own homes of whom almost 11 million are in the process of buying them using mortgage credit. The period since 1979 has seen substantial growth in home-ownership. There were several key influences. Housing policy was explicitly committed to the expansion of owner occupation, in particular, giving tenants of state housing the 'Right-to-Buy' their accommodation at discounts that could exceed 30 per cent of the market value. Between 1981 and 1991, 1.4 million additional homes were added to the stock of owner occupied houses through this process. At the same time, local state housing providers (local authorities) were precluded from re-investing the proceeds of such sales in further rental property. There were also fiscal incentives to enter home-ownership in the form of tax relief on the first £30 000 of mortgage interest (MIRAS), although this has been successively restricted during the l990s and was finally abolished in the March 1999 budget.

Realisation of the preference amongst the majority of British households to own their homes had, in the late 1970s and early 1980s, often been constrained by restrictions on access to credit. Legislation to allow financial de-regulation was passed in 1995 and this made a major contribution to meeting pent-up demand for home ownership. As the credit market became more competitive, lending criteria were relaxed and more households were able to buy their homes. The number of mortgage advances to first-time buyers in 1981 was 318 000, reaching a peak in 1986 of 619 000. Much of the expansion in home ownership was achieved by drawing in borrowers from the lower socio-economic groups who often had low paid jobs. Whereas in 1978 only 9 per cent of semi and un-skilled workers were home owners, by 1991, the figures were 42 per cent and 25 per cent. Currently, almost a third of mortgagors are in the bottom income decile.

2. The prerequisites of sustainable home ownership

Historically, there are two key factors that sustain the housing market and successful owner occupation in Britain; stable employment and an adequate safety-net. In particular, the nature of mortgage credit financing sets certain conditions. Households in Britain typically borrow over a

25 year period, and, on average, first-time buyers borrow 95 per cent of the purchase price. Variable interest rate products remain the most widely used form of finance.[1] In these circumstances sustainable home ownership firstly requires households to have secure and stable incomes allowing households to pay regularly and enabling them to respond to rapid shifts in interest rates. Home ownership is therefore predicated on widespread access to permanent and adequately remunerated employment. Sustainable home ownership also requires some 'safety-net' provision to enable people to meet their credit payments following unemployment due to redundancy, illness or accident or relationship breakdown. In Britain, since 1948, this has been provided as part of the state welfare system with borrowers eligible to claim subsistence benefits (currently Income Support or Jobseekers Allowance) receiving assistance with their mortgage interest payments. At the height of the recessionary period in the early l990s in Britain, this State safety-net assisted 556 000 households with their mortgage interest payments, many of whom avoided over-indebtedness as a result of this safety-net.

3. The emergence of unsustainable owner occupation

There are both structural and cyclical influences on the ability of households to manage the payment of their mortgage credit effectively and sustain their owner occupation. The more significant changes in the longer term are the structural ones and the discussion will be principally confined to the issue of structural change.

In Britain, the structures and relationships that have traditionally underpinned home ownership (well regulated, well rewarded and secure employment opportunities, alongside a State safety-net) are currently subject to re-structuring. Both these supports have been described as 'fragmenting' and 'unravelling' (Ford and Wilcox, 1994, 1998), in principle undermining the sustainability of home ownership and increasing over-indebtedness.

Over the last two decades, Britain, along with other western economies have experienced considerable restructuring as they have responded to and in turn influenced processes referred to collectively as globalisation. The associated risks to home owners stem from a re-structured labour market where unemployment is more prevalent and where there is an increase in the incidence of insecure and casualised employment and low waged work. All these changes create considerable financial insecurity for those caught up in them. To a considerable extent, these changes have been associated with the decline of the traditional manufacturing industries which offered full-time, skilled employment and the growth of part-time, unskilled service sector work. There are also significant changes in the forms of employment contract consequent on restructuring as employers seek to retain or enhance their competitiveness by transferring costs and responsibilities they previously met (pension and sickness provision, guaranteed hours, etc...) to their employees.

In addition, in Britain, State welfare provision has been under scrutiny on both ideological and financial grounds. As a result, Britain has seen the adoption of a policy of welfare markets with the presumption that individuals will increasingly bear the risks and responsibilities of making provision for eventualities that have traditionally been meet by the State (for example through the equity market for pension provision, and the insurance market for long-term care in old age). A key area of this welfare re-structuring has been the expectation that home owners will meet the costs of their mortgage payments following unemployment or sickness by taking out private insurance rather than relying on the State. To this end, State provision has been limited, first in 1987 and much more substantially in October 1995. The risks to home owners are those of too high a cost of market participation or rejection by the market.

Thus, the previously supportive structures of employment and safety-net provision that underpinned the housing market are changing and fragmenting. They are increasingly

1 The recent volatility in UK interest rates has resulted in some switch to fixet rate/fixed period credit products for house purchase. Variable rate credit, however, remains the norm.

characterised by uncertainty and insecurity and hence have the potential to place home owners and home ownership 'at risk'.

In these changing circumstances there are three key questions to be considered:

- To what extent are mortgage borrowers affected by the potential insecurities of economic re-structuring and by labour market risk?
- What is the evidence on over-indebtedness amongst mortgagors in these 'new' circumstances?
- How successful is the development of the private insurance based safety-net for mortgagors? Does privatised insurance provision for mortgage payments mitigate the effects of labour market insecurity?

4. Labour market risk

There are important conceptual and definitional issues surrounding the concept of labour market risk. Here, all forms of employment less than full-time, permanent employment are regarded as 'risky' or 'precarious', although clearly they are so to different degrees. One reason for defining risk in this way is that all these forms of employment have much shorter durations than full-time permanent employment, so the chances of labour market disruption and unemployment are greater. Recent analysis, for example, indicates that the average duration of self-employment is half that of permanent full time employment, and therefore riskier. Full-time temporary employment has an average duration of 10 months compared to three years for full-time self-employment and so, measured in terms of duration, riskier still (Gregg and Wadsworth, 1995). Risk also flows from any shift in the form of employment contract that reduces employment rights and safeguards. Thus, employment contracts that specify 'zero hours' are riskier than those with fixed and specified hours. In the former case, the hours of work can be varied in any time period without notice. This puts the stable budgeting required by a home owner if they are to be able to pay their mortgage at risk. Indeed there is evidence from studies of household decision making that households will often choose a lower but stable income because of the certainty associated with it.

Recent cross-sectional analysis of the Spring 1998 UK Labour Force Survey (Table 1) shows that about a quarter of mortgagor households are headed by someone either in 'precarious' or 'risky' employment or unemployed. The largest category is the self-employed, representing 15 per cent of mortgagor households. Two percent of mortgagor households were unemployed.

Table 1 – Employment status of heads of households in, or seeking employment, by tenure Winter 1997/98

	Mortgagor H of H %	Renter H of H %	All[1] H of H %
Full-time permanent employee	76	51	67
Part-time permanent employee	3	12	6
Full-time self-employed	14	11	14
Part-time self-employed	1	5	2
Full-time temporary employee	3	2	3
Part-time temporary employee	1	1	1
Trainee or unpaid family worker	-	-	1
Unemployed	2	18	6

Source: Labour force survey Winter (Dec 1997 — Feb 1998)
1 In addition to mortgagors and renters this figure includes outright owners, shared owners, those living rent free and squatting

Additional analysis of longitudinal data (British Household Panel Survey[2]) shows that over the period 1990-1995, a higher percentage of mortgagor households occupied a risk position. For example, 28 per cent had experienced at least one change of employment and of these almost a fifth had a period of self-employment. A third had experienced at least one spell of unemployment over the five year period (Ford, 1998). Other studies indicate that where unemployment is followed by re-employment, the odds of re-employment in a precarious job and/or in a lower wage job increase (Buck *et al.*, 1994; White and Forth, 1998).

The above (and other data) indicate that a large minority of mortgagors households are headed by someone already caught up in the re-structuring of the labour market whereby one of the key structures underpinning home ownership no longer offers the support it did previously. Evidence from surveys in Britain indicate that these changes contribute to over-indebtedness and this is discussed below. First, however, I will outline the general position with respect to mortgage over-indebtedness and then consider the causes of this situation drawing attention to the significance of the labour market changes discussed above.

5. Mortgage over-indebtedness in Britain

The extent of the problem

A series of studies in Britain indicate that mortgage over-indebtedness is a very serious issue with profound social and economic costs to individuals, families, creditors and the Government. These consequences include homelessness, relationship breakdown and separation of household members, severe emotional, psychological and physical consequences for both adults and children and over-indebtedness in non-housing areas. Over-indebtedness also has implications for the profitability of credit organisations, for consumer confidence and for the buoyancy of the housing market and the economy. These consequences are always significant at the level of the individual and household, but as the extent of over-indebtedness has grown so it has become a societal issue.

Over time, the overall trend in mortgage arrears has been an upward one. This trend, however, is also affected by the economic cycle. Thus, during the 1980s and 1990s, each peak of arrears was followed by a trough, *but* not by a return to the previously low level, as shown by Figure 1 below. At their highest point, in 1991, approaching a million households owed at least two months mortgage payments with approaching 100 000 owing 12 or more months payments. Since 1985, over half a million households have had their homes taken into possession by their lenders and become homeless.

The figures above are cross-sectional data, indicating the position at any one point in time. Evidence from a national, random sample survey shows that home owners move in and out of over-indebtedness and that between l991 and 1994, one in every five home buyers had missed some payments. Table 2 sets out the profile of this situation (Ford *et al.*, 1995). While, the position has clearly improved since the extreme difficulties associated with the early l990s where there was a conjunction of structural change and a severe cyclical recession, it is important to bear in mind that the problem is always greater than the cross sectional data suggest.

2 The British Household Panel Survey is a longitudinal survey of an initial 5000 households which includes annual interviews ('waves') with all adult household members. The members of separating households continue to be traced and included. Their new household partners in turn become part of the panel. Nine 'waves' of the survey have now been undertaken.

Figure 1 — Mortgage Arrears and Repossessions in Britain 1985 to 1998

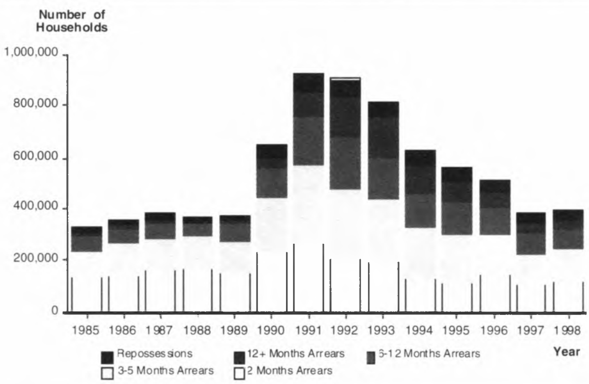

Table 2 – Moving into and out of mortgage arrears, 1991-1993

	% of all mortgagors
Arrears during 1991-1993, cleared and no current payment difficulties	3
Arrears during 1991-1993, cleared but some difficulty finding payments	3
Arrears during 1991-1993, cleared but currently in arrears again	1
In arrears for the whole of 1991-1993	1
Fallen into arrears for the first time 1991-1993	3
Total percentage of mortgagors experiencing arrears at some point during 1991-1993	11
Currently having some difficulty finding payment but with no current or past arrears	9

Source: *Ford et al.*, 1995

Although the figures for over-indebtedness in the late l990s are lower, it is important to bear in mind that at the end of 1998, 3.3 per cent of mortgagors were over-indebted and that others had been during the year. Further, the Survey of English Housing reported that in 1996/7 12 per cent of all mortgagors were finding it difficult to pay. In total, in 1996/97 approaching one in six households with mortgage credit had missed some payments or recognised that they were at risk of doing so.

The causes and characteristics of those who are over-indebted

Typically, over-indebtedness comes about for more than one reason. However, surveys that have asked respondents to indicate the main reason for their problems show that labour market change accounts for 60 per cent of the incidence of arrears. A quarter of all arrears result from job loss, l7 per cent from failed self-employment and 16 per cent from a reduction in earnings. By contrast relationship breakdown is significant in 14 per cent of cases and financial over-commitment in 7 percent of cases.

There is clear evidence from bi-variate analysis that the riskier labour market positions are associated with higher levels of over-indebtedness (Burrows and Ford, 1998). A higher percentage of owner occupiers in part-time employment or self-employment have mortgage arrears than do owner occupiers in full-time permanent employment. Unemployed home owners have the highest incidence of arrears, as shown in the table below.

Table 3 – Mortgage arrears by employment status of head of household 1993/4-1996/7

In arrears (% of each group)

	1993/4	1994/5	1995/6	1996/7
Full-time employees	5	3	3	2
Part-time employees	8	9	7	6
Small business owners	7	4	3	2
Self-employed sole-trader	12	8	6	8
Unemployed	24	19	22	19

Source: SEH 1993-1997 *(own analysis)*

Analysis using logistic regression techniques indicates that the relationship between the form of employment and arrears shown above holds after controlling for other variables. Compared to full-time employees, self-employed mortgagors, those in part-time work and unemployed home owners are significantly more likely to experience mortgage arrears. These relationships have remained significant across a period of time. A full account of the significance of a range of characteristics on the odds of mortgage over-indebtedness is provided as a table at the end of the paper.[3]

Surveys also show that a proportion of home owners are not over-indebted but are only meeting their credit payments with difficulty. Again, being in a risky labour market position increases the odds of payment difficulties. Unemployed people and self-employed home owners were particularly likely to report difficulties meeting their payments.

Thus, in Britain the evidence points strongly to the significance for home owners of the changes occurring in the labour market. These developments clearly challenge sustainable home ownership. Further, labour market assessments to the year 2010 indicate a continuation of the current labour market trends. However, potentially, the impact of these trends on home owners could be mitigated by the provision of a comprehensive 'safety-net' and this issue is discussed in the next.

6. Safety-net provision for home owners

Britain has both a State and a private insurance based safety-net system available to assist home owners who become over-indebted as a result of unemployment, accident or sickness. In addition, the State system (ISMI) can help home owners who become lone parents as a result of separation and divorce. The State system restricts eligibility to those home owners who also claim subsistence benefit. This State safety-net was created in 1948.

During the 1980s, fiscal and ideological factors led to a shift in policy towards State assistance to home owners who lost all income and the safety-net has been curtailed twice. First in 1987 and again more substantially in October 1995.[4] The policy objective with respect to safety-net provision for home owners was that owners should take responsibility for safety-net provision by taking out Mortgage Payments Protection Insurance (MPPI) supplied by the private insurance

3 See Table on Logistic Regression Models of the Odds of being in Mortgage Arrears for 3 or more months.

4 The current position is that mortgagors eligible for subsistence benefits and who took a mortgage after October 1995 receive no assistance with their mortgage payments for 9 months. Full eligible costs are paid thereafter. Pre-October 1995 borrowers who qualify receive no assistance for 2 months, 50 per cent of eligible costs for the next four months and full eligible costs thereafter. The restrictions on eligible costs have also been tightened for all claimants.

market. The argument was that the restriction of ISMI would, *inevitably,* support the development of the private welfare market.

In practice, the take up of private Mortgage Payments Protection Insurance has been limited and slow. Around 25 per cent of those with mortgage credit have this insurance but there is no evidence that take-up is concentrated amongst those that carry the greatest risk of losing their income or who have the fewest resources available to them should this happen. Current developments confound theories of insurance with their rational choice assumptions that predict the need to guard against adverse selection and moral hazard. Currently, UIC home owners are cautious about the private insurance product and the providers. The lack of statutory regulation is clearly one problem but so too is the miss-selling record of some sections of the insurance market and the exclusionary conditions that are applied by some insurers. The potential, however, is for the market to offer cover to a far greater proportion of home owners than does the State.[5]

The issue though is not just that of improving take up of private insurance, but concerns the effectiveness of the safety-nets only if they provide support when needed will they sustain homeowners. A recent evaluation of both the State and private safety-nets indicated that, following a successful claim, neither safety-net necessarily precluded over-indebtedness (mortgage arrears). In twenty percent of cases of home owners claiming on the private safety-net, the system was not able to prevent the over-indebtedness that could result in a threat to the maintenance ofthe home. However, the private safety-net is currently a more effective means of sustaining home ownership than is the State safety-net where more than 40 percent of those receiving it could not meet their mortgage payments. For both State and private safety-nets, significant minorities of home owners either received less from the safety net than they had to pay to their mortgage lender and/or had to wait a considerable period of time before they qualified to receive payments which werethen not backdated. The general conclusion fromthis workis that, currently, neither the state nor the private insurance market provide a comprehensive or fully effective safety-net to assist home owners and, in a proportion of cases, the structure of these safety nets actually contribute to the development of over-indebtedness.

As the labour market becomes riskier the need for an effective safety-net becomes more rather than less important if home owners are to avoid over-indebtedness. The current situation in Britain indicates that both of the pre-requisites of sustainable home ownership — stable, secure incomes and adequate, effective safety-nets — are fragmenting and unravelling and contributing to the growth and persistence of unsustainable home ownership.

7. The relevance of the UK experience to other European countries

This paper has been about the emergence of mortgage over-indebtedness in Britain, and the paper did not set out to offer a comparative analysis. Nevertheless, the key structures and processes that are underlying the changes for home owners in Britain are also operating in other countries. Most if not all European countries have experienced an expansion of home ownership, if from rather different starting points.

Currently the percentages of home ownership vary, for example, in Germany home ownership is around 40 per cent, in France 54 per cent, Sweden 42 per cent and Portugal 58 per cent. The percentages buying their homes with credit also varies nationally as does the amount that can be borrowed, the terms and conditions of the credit and the time period over which borrowing takes place.

5 Currently, under 5 per cent of mortgagors are being assisted to meet their mortgage payments through the State system-Income Support Mortgage Interest (ISMI) with around 25 per cent likely to be eligible to claim from the State should they loose all income. Only one percent of mortgagors are currently meeting their mortgage credit payments through such insurance, although potential the MPPI market is much larger than the number eligible to claim on ISMI.

Equally, globalisation and international economic competitive pressures are, by definition, ubiquitous and hence their impact cannot be avoided. National backcloths and strategies towards economic re-structuring, however, vary. Thus, within the same broad trends there will be differences in the strategies used towards the achievement of competitiveness. As a result the impact on national labour markets will differ as will the scope for varying forms of intervention. As one analyst has noted 'a country can control the form and distribution of risk but cannot evade it' (White, 1996). Analysts such as Esping-Anderson (1996) have developed a 3-fold typology of strategic responses to the challenges of globalisation, industrial decline and unemployment: the Scandanavian response; neo-liberal (US, Britain) and labour reduction responses (Germany, France). Thus there are predicted and observable differences in national strategies. In the labour reduction model and the Scandanavian model the emphasis is on retaining tighter labour market regulation and consequently a high wagefhigh unemployment economy. The neo-liberal response pursues maximum de-regulation (consistent with EU Directives) resulting in economies with low wages, casualised terms and conditions of employment and rapid labour turnover. These changes produce different forms and balances of risk which impact on differently structured systems of home ownership finance creating a range of potential problems for home owners.

There is also a range of approaches to welfare provision which again, even within a common fiscal crisis, result in different abilities and willingness in different countries to protect individuals against labour market and housing market disadvantage. This variation in welfare regimes has also been captured in conceptual and theoretical models one such based on the extent to which welfare systems protect people irrespective of their resources or labour market position. Thus, for example, the UK is characterised as a Liberal welfare regime with a strategy of reducing welfare support both in terms of the amount offered and the groups of people eligible to receive welfare, as opposed to the Social-Democratic welfare model followed in the Nordic countries that offers more generous and widely based welfare provision (Esping-Anderson, 1990). The differing welfare structures and responses can mitigate or increase the expose of households to economic and labour market risk which as already discussed is a product of a countries strategic response to economic re-structuring. These two sets of strategic responses will influence the extent to which home ownership becomes unsustainable and with what consequences. The UK experience may prove to be more extreme than that in some other countries (lax employment regulation and a reducing commitment to state welfare in favour of non-compulsory reliance on provision through the private market) but it clearly exemplifies the structures and processes that are operating to shape events in many countries.

In conclusion, therefore, there is considerable evidence that as home ownership rates have edged up in most European countries and mortgage credit expanded, the conditions for the successful implementation of home ownership are less certain. In some countries, notably Britain (but not only there), the problems are quite marked. There are profound outcomes and implications for individuals and households in the form of growing homelessness, poverty, unhealthy lives and social exclusionary processes. There are serious implications for national governments in terms of them pursuing a housing policy towards home ownership that fails to consider its limits in the context of other policies and the potential damage to the macro economy from too high a level of failure in home ownership. There are also implications for national governments in having to respond to homelessness and disaffected home owners at the political and social levels.

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Table – Logistic Regression Models of the Odds of Being in Mortgage Arrears for 3 months or more

Variable	N	Bivariate	N	Best Fitting
Base Odds for paradigmatic Case	8424	Varies	8070	0.004
Employee or Self-Employed				
Employee	6679	1.00	6523	1.00
Self-Employed	1588	1.93***	1547	1.78***
Marital Status				
Not Divorced or Separated	7673	1.00	7355	1.00
Divorced or Separated	751	2.39***	715	1.76*
Current Employment Status of the HOH				
Employed Full Time	6917	1.00	6753	1.00
Employed Part Time	343	2.81	336	2.90***
Unemployed	374	9.63***	375	7.96***
Retired	397	1.02	331	3.94*
Unable to Work		3.45***	275	4.49***
Type of Household Structure				
Couple. No Dependent Children	3440	1.00	3296	1.00
Couple. With Dependent Children	3238	1.79***	3130	1.56*
Lone Parent	295	3.84***	263	1.23
Large Adult Household	397	2.62***	372	1.48
Single Male	563	2.80***	551	1.92*
Single Female	491	0.92	458	0.65
Social Class of HOH				
I. Professional-Managerial	881	1.00	870	1.00
II. Intermediate	2844	2.88**	2798	2.52*
III. Skilled Non Manual	1034	2.85*	1018	2.02
IV. Skilled Manual	2435	4.42***	2395	3.46**
V. Semi-Skilled Manual	824	5.39***	810	3.43**
VI. Unskilled Manual	186	5.65***	179	2.80
Age of Head of Household (HOH)				
18-24	226	2.03*	221	3.38*
25-34	2174	1.27	2100	1.31
35-44	2624	1.31	2523	1.22

(contin.)

Variable	N	Bivariate	N	Best Fitting
45-54	2144	1.00	2068	1.00
55 –64	960	0.59	902	0.38**
65+	296	0.68	256	0.21*
Region				
Provinces	5310	1.00	5086	1.00
South East	2096	1.35*	2011	1.56**
Greater London	1018	1.47*	973	1.46
First Time Buyer?				
No	5034	1.00	4850	—
Yes	3376	1.48**	3220	—
Seller				
Not LA. New Town or HA	7487	1.00	7196	—
LA. New Town or HA	928	1.75**	874	—
Type of Mortgage				
Capital and Interest	7269	1.00	2647	1.00
Interest Only	1137	0.57***	5423	0.52***
Mortgage as % of Purchase Price				
Not 100%	7269	1.00	6984	1.00
100% Mortgage	1137	2.25***	1086	1.93***
Type of Mortgage Lender				
Building Soc. LA or Insurance Co	7149	1.00	6863	1.00
Bank	1139	0.74	1081	062*
Someone Else	132	2.21*	126	1.97
Year Current House Purchased				
Pre-1987	3906	1.00	3740	1.00
1987-1989	2145	1.83***	2066	1.84***
Post-1989	2373	1.11	2264	1.20