Better connections, better business.

Mortgage Efficiency Survey 2019

IRESS.COM/MES2019

Foreword

Over the past eight years, the Iress Mortgage Efficiency Survey has been exploring the impact of technology on the mortgage market. Last year, we concluded the new wave of technologies such as open banking and application programming interfaces (APIs) are delivering a more connected mortgage ecosystem. This has proven to be a dominant theme this time around, too. It is clear technology is set to underpin the evolution of the UK mortgage market in years to come but how fast is it moving and is the industry actually getting better connected?

The speed of innovation means those who grasp and embrace emerging developments will be best placed to improve the consumer experience. Those who ignore or fail to harness new and improved technologies in the mortgage market risk being left behind.

Steven Carruthers

Principal Consultant, Mortgages

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Findings at a glance

Making the right connection

- More than half of lenders expect application programming interfaces (APIs) to provide the most transformative efficiency gains over the next three to five years
- Over two thirds of lenders are considering or actively reviewing mortgage hub technology
- More than three-quarters of firms have already implemented or are pondering the implementation of open banking
- More than two thirds of lenders are either considering or have already implemented mobile services for their proposition features
- Some 59% of lenders are considering, actively reviewing, likely to or have already implemented early decisioning functionality
- An increase has occurred in the number of firms considering or actively reviewing artificial intelligence and machine learning technology to support propositions.

It's never been easier to switch

- Product switching continues to exert its dominance on existing mortgage business activity
- The number of lenders offering online product switching for intermediaries has leapt by almost two-thirds
- Online product switch recommendations continue to rise: Some 77% and 82% of lenders surveyed now offer this service for consumers and intermediaries respectively
- Six out of ten lenders now also offer, or plan to offer, further advance product switch or mobile app online services for intermediaries and their clients
- Almost two-thirds of lenders are offering online product switching for intermediaries

Eye-catching data

- An increase in consumers taking five-year fixed rate products could impact the volume of remortgages and product transfers in the short to medium term
- The number of offers being produced in shorter timescales has increased year on year, with less offers being produced over longer periods
- Telephony has increased by a third from last year but direct distribution through consumer (digital) channels has fallen by 75%

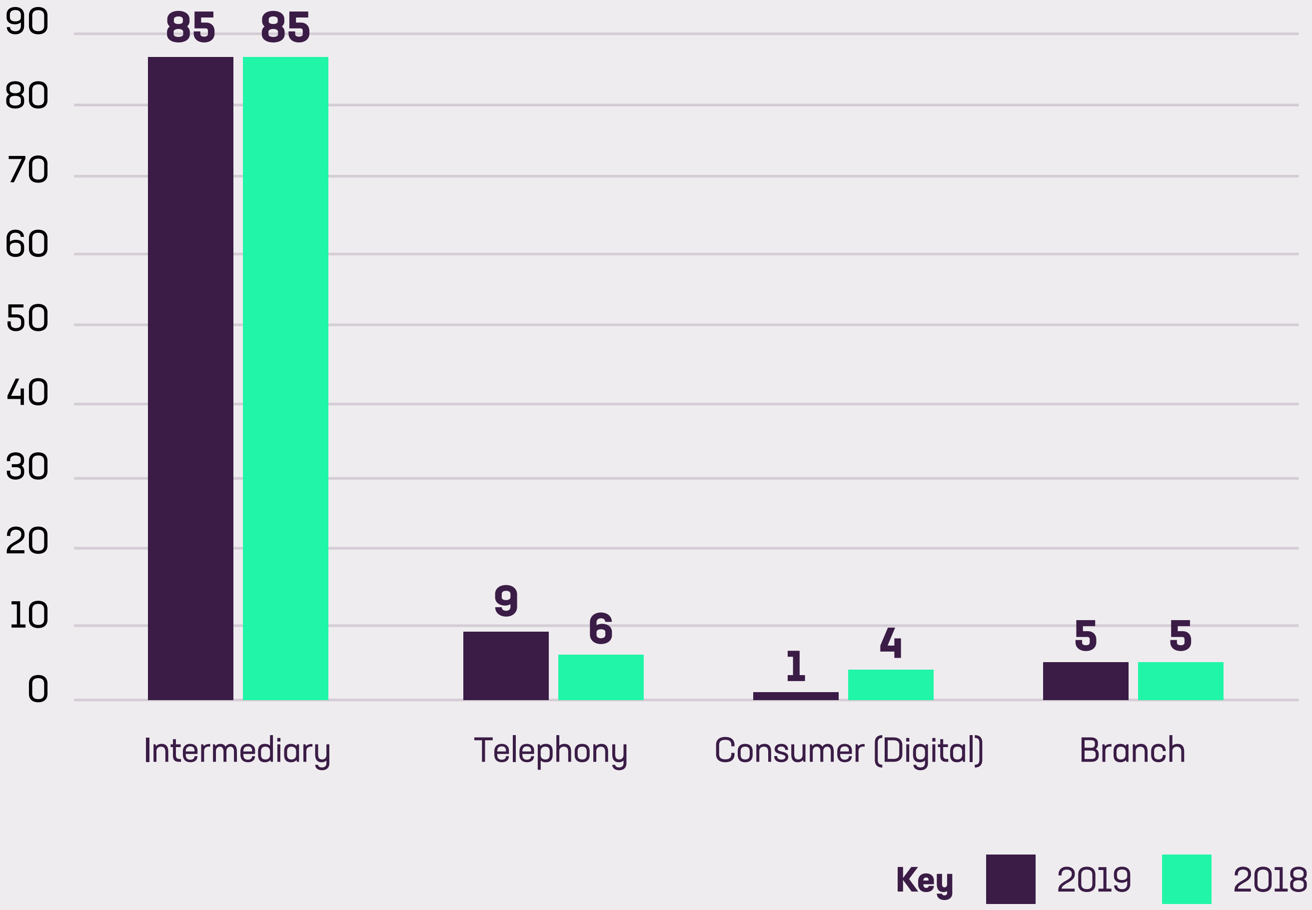
We hope you enjoy reading the full report.

Sales distribution

Distribution through intermediaries, at 85% again in 2019, continues to be the main route to market for the majority of the lenders who participated in this year's survey. It is widely recognised in the wider market that the current split of distribution is one of 75% intermediated and 25% direct. This split may change in favour of direct distribution over the next five years as impacts from new technologies, product transfers, regulation and execution only are realised.

Telephony has seen a 33% increase in the past 12 months and direct distribution through consumer (digital) channels has surprisingly dropped back by 75% since last year. The increase in telephony is possibly as a result of lenders investing in lower cost distribution and sales channels combined with consumers starting their journey online and moving into telephony for advice. This would also account for the reduction in the digital distribution channel. Another potential reason for an increase in telephony distribution is where consumers are staying with their existing lender at the end of their product deal period, utilising lenders' product transfer/rate switch offering direct.

Sales distribution %

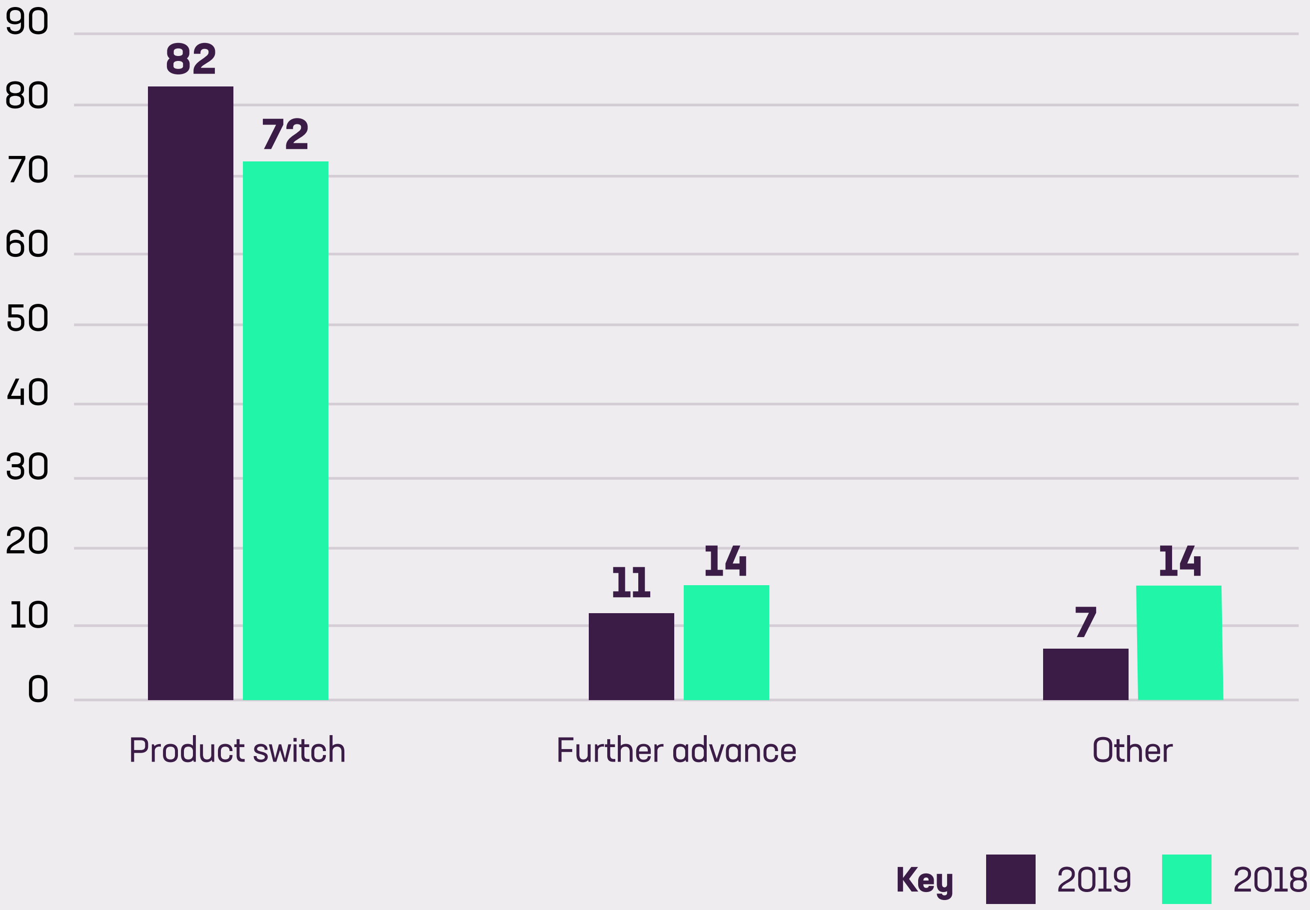


Product switching

Switching a client's mortgage product, also known as a product transfer (PT) or rate switch, typically at the end of a preferential term, is the largest part of existing mortgage business activity for lenders. The figure has jumped ten percentage points to 82% in the past 12 months alone, equating to £80.6bn at the end of H1 2019 vs £74.8bn in the same period last year. According to UK Finance data the product switch market was worth £158.7bn in 2018. So far in 2019 PT's have accounted for £41.4bn in Q1 and £39.2bn in Q2. Further advances, meanwhile, have dropped from 14% to 11%. Other transactions have also witnessed a sizeable fall – halving from 14% to seven per cent.

Market commentary has indicated that while PTs have grown significantly over the last two years, the increase in consumers taking five-year fixed rate products (given the relative competitive pricing versus two-year fixed rate products) could impact the volume of re-mortgages and PTs in the short to medium term. This may present some intermediaries with a challenge in terms of fee income, particularly should lenders move to acquire more PT and remortgage business through lower cost direct channels, either advised or on an execution only basis.

Existing mortgage business activity %



Accepts, declines, refers

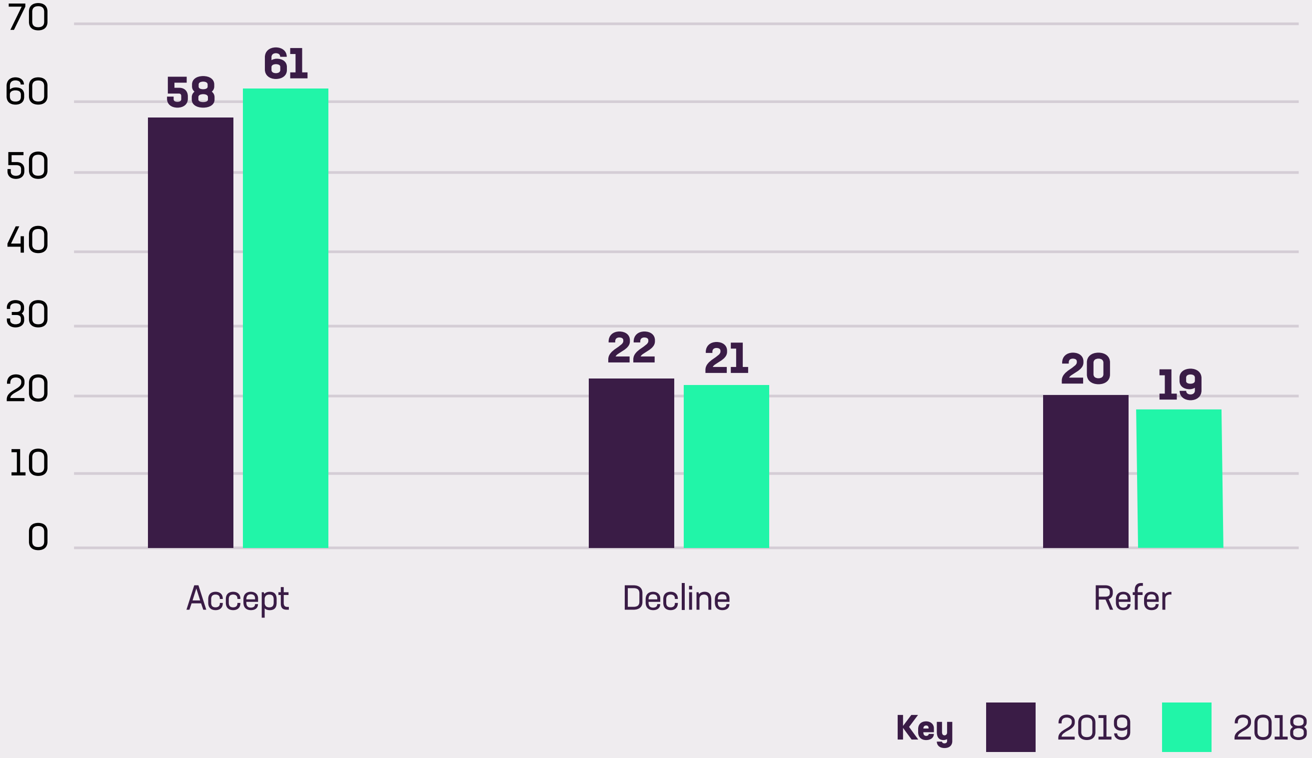
Securing a decision in principle (DIP) accept for an application is a key point in the mortgage buying process, both for mortgage intermediaries and their clients. Receipt of an approved DIP provides greater certainty and understanding early in the process and helps to manage expectations for everyone involved. Accepts in the intermediary channel decreased by almost six per cent from 2018 to 58%. Declines, meanwhile, increased by five per cent to 22% over the same period. Refers also saw a five per cent uptick in 2019 versus 2018.

In the direct (branch and telephony) channels, accepts decreased from 49.5% in 2018 to 45% in 2019. Declines and refers, however, headed in the opposite direction - increasing to 18% from 14.5% and to 38% from 36%, respectively.

Both the intermediary and the direct distribution channels have seen a decrease in accepts and an increase in declines and refers. This could point to lenders' reduced appetite for risk in what is currently a highly competitive market and one where lending margins are significantly reduced. Anecdotal feedback indicates that many lenders are focusing on greater quality lending and less volume. Continued investment in more sophisticated early decisioning technology allows lenders to be more selective. Equally, many lenders retain a USP of human underwriting who take risk based decisions. This may account for the increase in refers as lenders consider consumers with more complex needs.

“Direct channels have the highest referral rate of 38%.”

Intermediary accepts, declines, refers %

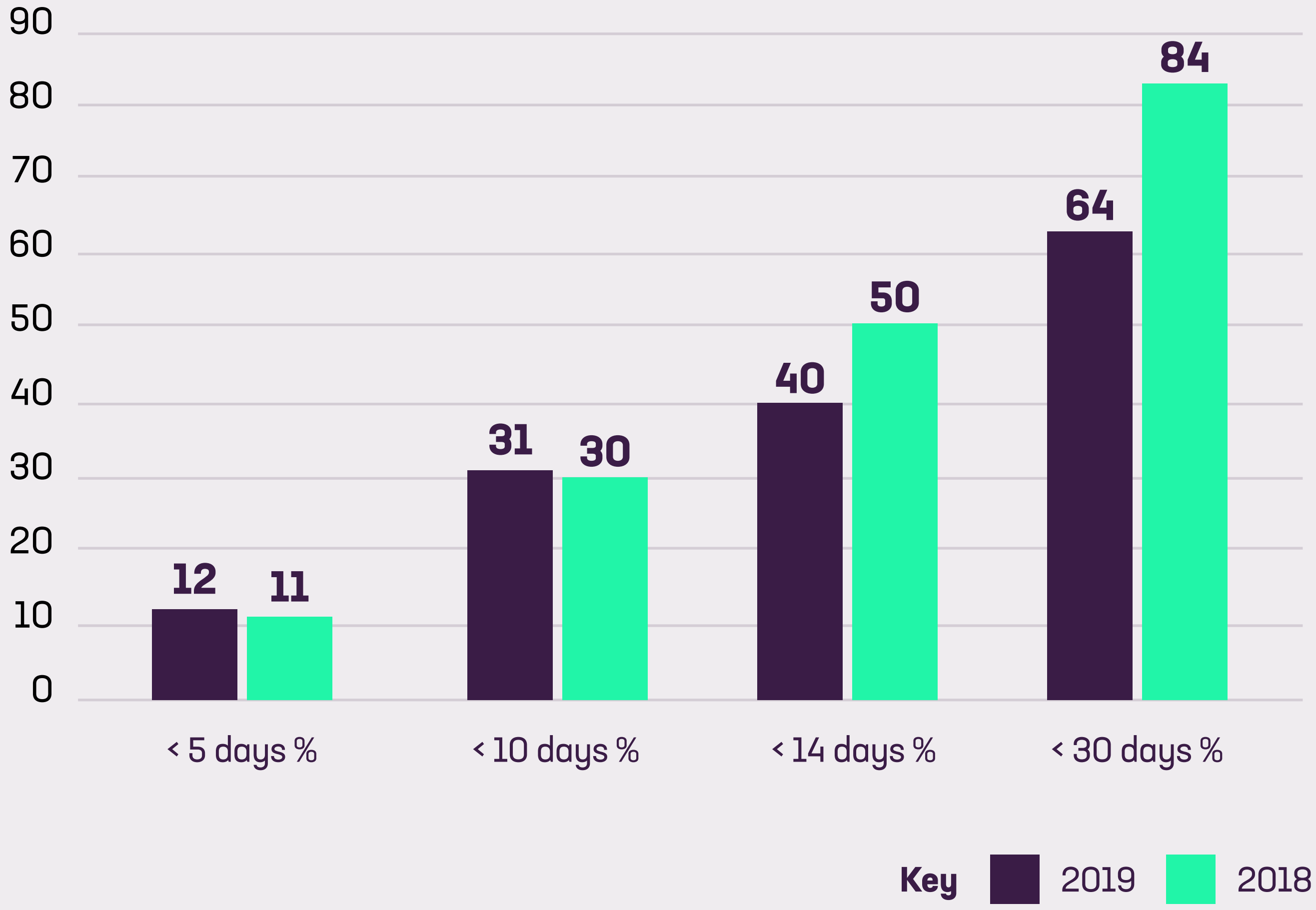


Days to offer

In the number of offers produced in under five and ten days respectively, as speed to offer timescales are improving, there has been a reduction in the number of offers over the longer periods of up to fourteen and thirty days. Market feedback suggests that continued investment in technology is improving offer timescales. On the flip side, full API connectivity to third party stakeholders (e.g. ID&V providers, valuation panel managers, credit bureaus) is not consistent across the lender community and offers opportunity to further improve offer timescales.

> **"Slightly faster offers but still room to improve."**

Days to offer %



Emerging technologies

Digital online services

The provision of online digital services to consumers and intermediaries continues to develop as lenders harness and evolve new technologies and platforms to meet customer needs.

With higher levels of product switching year on year, more lenders have implemented an online digital service to meet direct consumer and intermediary needs. Some 77% of lenders surveyed now offer an online product switch proposition for consumers, and for intermediaries 82% of lenders offer the service online.

In addition, 61% of lenders now also offer, or plan to offer, further advance product switch or mobile app online services for intermediaries and their clients.

However, over two thirds (68%) of respondent lenders have no plans to offer a mobile app for intermediaries. Market feedback indicates that intermediaries' preference is to communicate direct through lender portals or via business development field and telephony teams.

"There has been a 64% increase in lenders offering online product switching for intermediaries."

Voice activated services

Today, an estimated 600 million people use voice activated assistants at least once a week, globally. A September 2018 study of U.S. consumers by Adobe* revealed the high retention rate of voice searchers, with 44% saying they utilise voice assistants several times a day. The rise of voice-activated services, particularly for searches, has been spurred by advances in voice-recognition technology, consumer demand for convenience (it's quicker and easier than typing) and the evolution of personal voice assistant devices such as Amazon Alexa, Apple Siri and Google Home. By 2020 it is expected that half of all searches will be voice activated. Our survey examined whether UK lenders are considering this technology to engage with intermediaries and consumers.

Just over a quarter (27%) of lenders surveyed (down from 33% in 2018) are considering voice activated services with the majority of lenders (68%) not considering this technology. Less than one in twenty lenders (4.5%) stated they were likely to implement.

Lenders commented that voice activated services could provide cost and time efficiencies, an additional broker communication channel for progress updates and also meet consumer engagement preferences given the increased utilisation of this technology across other markets. Lenders also commented that while this communication channel could add value, it is much lower down the IT development priority list at this stage with more resource and investment being concentrated on building and providing API

*cmo.adobe.com/articles/2018/9/adobe-2018-consumer-voice-survey.html#gs.ei9u29

Mobile services

Brits used their smartphones to spend nearly a billion pounds at the checkout last year - a 328% year-on-year rise, according to figures from Worldpay*. Through the likes of Apple Pay, Google Pay and Samsung Pay, the number of in-store contactless transactions made via mobile devices totalled 126 million last year, with the total spend topping £975 million. Almost a third of consumers are now taking advantage of their phone's payment capabilities, according to Worldpay, which predicts exponential growth over the next 12 months.

Successive Iress surveys have shown a steady increase in mobile service provision for both consumers and intermediaries in the mortgage market. The use of mobile services to undertake financial transactions continues to grow with many service providers, retailers and banks/building societies offering mobile contactless payment facilities at point of sale or service.

More than two thirds of lenders are either considering or have already implemented mobile services for their proposition features, including for quotes, applications, case tracking/updates and product switches. The remaining third (32%) are not currently considering this technology. Commenting on the provision of mobile services, most lenders described this as a service driven by engagement preference which allows both broker and consumers to have a constant and instant view of their mortgage transaction.

*finextra.com/newsarticle/31753/uk-contactless-mobile-payments-hit-tipping-point

Open banking

Open banking is the practice of sharing financial information electronically, securely, and only under conditions that customers approve of. Application programming interfaces (APIs) allow third-parties to access financial information efficiently, which promotes the development of new apps and services. Open banking should result in a better experience for lenders, intermediaries and consumers. Lenders should be able to make more accurate lending decisions over quicker timescales which manage expectations earlier for intermediaries and consumers. As lenders become even more adept at using credit modelling, and depending on their risk appetite, they may incorporate open banking to develop bespoke product pricing based on an individual's specific income and expenditure profile (as opposed to using ONS data). From an advice perspective, it should reduce the amount of time collecting and keying data and allow for more time with customers who want or need advice.

January 2019 marked a year since open banking came into play in Europe. Although 2018 saw a steep learning curve for all involved, it remains to be seen whether the next two years show serious, market-defining transformation. Furthermore, will mortgage lenders manage to capitalise on new ways to stay relevant in the digital era? Firms such as Token, Yolt and Barclays were among those to claim 'firsts' powered by open banking in 2018, enabling easier payments and smarter money management for consumers. Meanwhile, M&S Bank, Bluestone Mortgages and Freedom Finance all announced implementation of an open banking service for their mortgage lending.

Just under two thirds (63%) of respondents are either considering (36%) or actively reviewing (27%) open banking with five per cent already implementing/implemented and nine per cent likely to implement. That said, nearly a quarter (23%) are currently not considering the service.

Application programming interfaces (APIs)

An API is a software 'translator' that allows two applications to talk to each other. In other words, an API is the messenger that sends a request from one software programme to another and delivers a response back. APIs provide sets of routines, protocols, and tools for building software applications.

In the mortgage market, more lenders are now using APIs to connect their digital platforms internally as well as with external third parties and to develop new innovative technology solutions. Lenders are building and implementing APIs to create efficiencies across the end to end mortgage journey. For example, reducing the amount of data being keyed and validating data in real-time. APIs can and do provide secure and trusted data sources for key elements of mortgage processing such as income and expenditure verification, sourcing and intermediary CRM connectivity and integration with third parties such as AVM providers, solicitors and the Land Registry.

Of the lenders surveyed, over half are actively reviewing or likely to implement APIs for income and expenditure verification, with 32% of lenders considering implementation. For other types of value-added services (e.g. connectivity to a third party interface), 40% of lenders are considering or actively reviewing APIs and 60% are likely to implement or have implemented APIs.

> **"More lenders are now using APIs to connect their digital platforms internally as well as with external third parties."**

Early decisioning

To help intermediaries recommend and place clients with the most appropriate lender for their needs, lenders continue to develop early decisioning technology that rules clients in or out much earlier in the process, therefore offering more accurate expectations. Using this type of technology means intermediaries can avoid running individual affordability and eligibility checks with several lenders portals offering a substantial time saving.

Enhanced early decisioning can improve the quality of applications, provide a quicker more efficient experience with greater certainty and transparency for intermediaries and their clients.

Some 59% of lender respondents are considering, actively reviewing, are likely to or have already implemented early decisioning functionality.

Instant messaging

WhatsApp, Facebook Messenger, Snapchat and iMessage are just some of the software applications that are now used on a daily basis across the globe as a key method of communication across a wide demographic of consumers on a multitude of technology devices such as smartphones, tablets and laptops.

Intermediaries and consumers are driving demand for increased real-time instant messaging as part of their engagement with lenders throughout the mortgage application end-to-end journey. Lenders commented they believe instant messaging technology allows them to provide more timely and quicker updates, reduced processing times and the ability to offer system generated event driven messages in real-time.

Just under half of the lender respondents are considering or actively reviewing instant messaging services for consumers with 15% likely to implement or already implementing the service. For intermediaries, 58% of lenders are considering or actively reviewing with just under a quarter of lenders (22%) likely to implement or already implementing instant messaging.

"Intermediaries and consumers are driving demand for increased real-time instant messaging as part of their engagement with lenders throughout the mortgage application end-to-end journey."

Mortgage hub technology

A key desire for everyone involved in the end to end mortgage journey is minimising the amount of re-keying and transfer of data. Mortgage hub technology allows intermediaries to source products for clients and connect through to lenders digitally without having to re-key or have multiple steps in the fact find, DIP and application process. Lenders recognise the value for themselves, the intermediary and their clients in making the journey as slick and efficient as possible with considerable cost and time savings possible through implementation of a more connected journey.

Lenders describe the benefits and efficiencies of mortgage hub technology as being vital to their propositions and enabling reduced data re-keying, quicker submissions and processing times, offering wider distribution and preserving data integrity. Lenders also anticipate a more connected, efficient and integrated journey from intermediary CRM, to product/criteria sourcing, to DIP, application and through to completion.

Over two thirds (70%) of lender respondents are considering or actively reviewing mortgage hub technology with 20% likely to implement or have already implemented.

“7 out of 10 respondents (70%) are engaged in the assessment of mortgage hub technology.”

Credit modelling

Risk management is a core function of all mortgage lenders and is a key area regularly scrutinised by the UK financial regulators. Credit modelling helps lenders manage risk and allows for a more complex, rich set of decision criteria using scorecards and models. The decision making process can be enhanced through credit modelling to improve risk management and provide products tailored to meet an individual's risk profile.

Describing the benefits of credit modelling, lenders believe a more detailed analysis of both the current financial history of a customer as well as the likely future loan performance can be assessed, more consistent, accurate and faster lending decisions can be made and quicker offers produced.

Half of the lender respondents are considering or actively reviewing credit modelling with almost a fifth (19%) likely to implement or have already implemented.

AI and machine learning

The birth of AI can be traced to a Dartmouth research project in 1956 that explored topics like problem solving and symbolic methods. In the 1960s, the US Department of Defence took interest in this type of work and increased the focus on training computers to mimic human reasoning. While machine learning is based on the idea that machines should be able to learn and adapt through experience, AI refers to a broader idea where machines can execute tasks 'smartly'. AI applies machine learning, deep learning and other techniques to solve actual problems.

In the mortgage market, AI and machine learning continues to be an evolving process. Fintech organisations, lenders, distributors, trade bodies and regulators are all collaborating to understand how this technology is being adopted to support and enhance the mortgage journey. Lenders expect AI and machine learning to take a lot of the heavy lifting out of the mortgage application process, creating efficiencies, reducing costs and allowing for a more personalised approach to consumer needs.

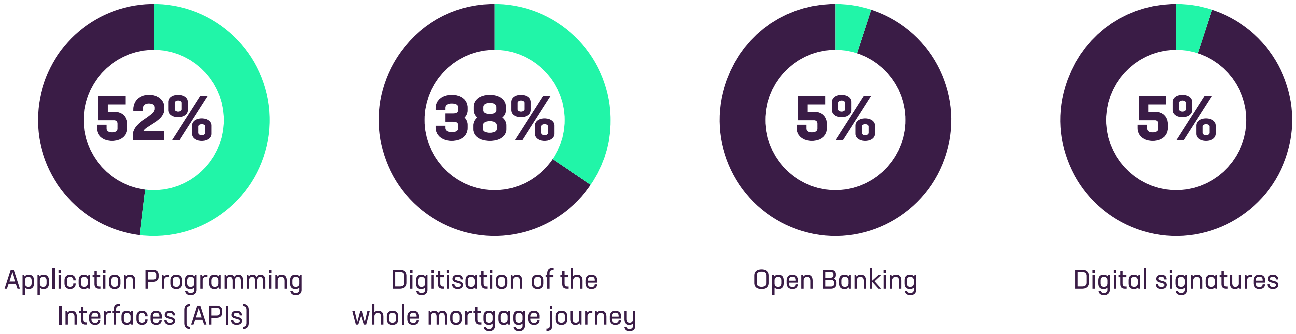
The survey found that over a third (36%) of lender respondents are considering or actively reviewing AI and machine learning technology to support their propositions. Just under a fifth (18%) are likely to implement or have implemented this technology, whereas 45% of lender respondents are not currently considering it. Similar to voice activated services, lenders said that although current focus is on API development and connectivity, AI and machine learning is likely to gain greater traction in the medium to longer term.

“Over a third (36%) of lender respondents are considering or actively reviewing AI and machine learning technology to support their propositions.”

Emerging technology drivers

The survey asked lenders to review a list of emerging technology drivers and to select those which they believed would provide the most transformative efficiency gains over the next three to five years.

Two technology drivers received 90% of the votes with over half (52%) of respondents' votes going to Application Programming Interfaces (APIs), which is consistent with last years' survey and reflects lender commentary as a key technology they are actively reviewing or implementing. A high proportion of lenders believe that the digitisation of the whole mortgage journey will be a key technology driver.



Conclusion

Technology continues to disrupt numerous industries, and the mortgage market is no different. Mortgage providers are clearly utilising tech to sharpen their focus on consumer experience - the various and expanding means of technology are fundamental to the improvement of this. But looking forward, there are some key tells from the data shown throughout this report that some technologies are anticipated to play a bigger part than others. The vast array of options, plus cost and resource, means lenders will have to prioritise.

What has also been apparent over the past 12 months is that a shift is occurring, anecdotally at least, to a focus on quality over quantity. This only serves to reinforce the view that consumer needs are being placed front and centre of mortgage propositions, and will be an interesting theme to monitor over the coming years.

But while the tech surge is likely to continue on its current trajectory, there is evidence this time around of the importance of people to the mortgage process; the sizeable jump in telephony being a case in point. The human and machine combination could be pivotal to powering the consumer mortgage journey in the future. Never has it been a more important time to get connected.

Appendix

Participants

23 lenders with a combined gross lending of circa £104bn*, and a market share of 39%*, participated in the 2019 survey. They represent a cross section of the UK mortgage market from specialist lenders, regional building societies, new entrants and high street names.

Atom Bank; Cambridge Building Society; Clydesdale Bank; Coventry Building Society; Cumberland Building Society; Dudley Building Society; Fleet Mortgages; Foundation Home Loans; Hinckley & Rugby Building Society; Leeds Building Society; Leek United Building Society; Marsden Building Society; Nationwide for Intermediaries; Newcastle Building Society; One Savings Bank; Santander; Skipton Building Society; The Co-operative Bank; The Mortgage Works; West Bromwich Building Society; Tipton & Coseley Building Society; Vida Homeloans; Virgin Money.

*Based on 2018 figures taken from UK Finance Largest Mortgage Lenders Table MM10.

Methodology

In general, an average figure has been used to illustrate patterns across the mortgage market and lender types. Iress has taken all reasonable care to provide clear and accurate statistics based on the data provided by each participant. Please note that the data provided by the participants has not been independently verified.

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Lender market tier groups are based on the UK Finance 'largest mortgage lenders by gross lending' table (MM10) and individual lenders' own published lending figures. The three tier groups are: Tier 1 lenders with more than 5% market share; Tier 2 lenders with more than 0.5% but less than 5% market share; and Tier 3 lenders with less than 0.5% market share.

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At Iress, we believe technology should help people perform better every day. Since our beginning in 1993, people across financial services have trusted us to take their performance to the next level. From the world's most iconic financial brands to entrepreneurial advice firms, challenger banks and digital disruptors, we help improve every aspect of your business so you can work better, every day.

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