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Chapter: 1

1.0 Introduction

Mortgage market in the United Kingdom has reported a dramatic transformation over the past few decades. This was contributed by a number of factors among them includes the regulatory changes in the banking sector. Essentially, house prices are important elements in the mortgage market that have seriously affected lives of many people in the UK. When undertaking a close examination of the general housing market, as well as, house prices, considerations should be place on factors influencing price determination and how it affects lives of people (Aoki, Proudman and Vlieghe, 2001). The United Kingdom mortgage market has in the past years reported both systematic and regulatory changes in the sector. In fact, the last crash in the UK housing market was experienced in the early 90s. However, since then period, there was a shift in the market trends, in which, house prices went up steadily. The peak price was registered in the year 2007 however, a declining phase followed thereafter during and after the financial crisis.

Similarly, scrutiny of the mortgage market has been done in many countries. There has been a fast pace increase in the house prices and to a great extent, many countries reported overvalued prices. The over-valuation posed enormous consequences and acted as a hindrance to people who wanted to purchase properties (BBC News, 2003). Buyers had no option, but to go for bigger mortgages. In the process, most of the players in the industry were engaged in the remortgaging of houses in order to acquire more money. They believed that if prices continue to climb up, they would eventually rip bigger returns. This was a similar scenario which was reported in the UK mortgage market; however, several regulatory measures in the banking sector reversed the entire process. In the real sense, there are a number of factors that affected the steady rise in the house prices (Ball, 2006). These include demand, supply and to the some extent, the mortgage lending. Alternatively, all these factors played a key role in the collapse of the UK mortgage market. This implies that the 2008 collapse in the housing market was cause by miscalculation in the side of financial lenders, as well as, poor management of the mortgage market. Based on the above introduction, this paper sought to examine banking regulations in the UK and how it affected the mortgage market. This will be accomplished by examining five main banking institutions namely Barclays Bank, HSBC, Lloyds, Santander Bank Plc. and Natwest Bank.

1.1 Background Information

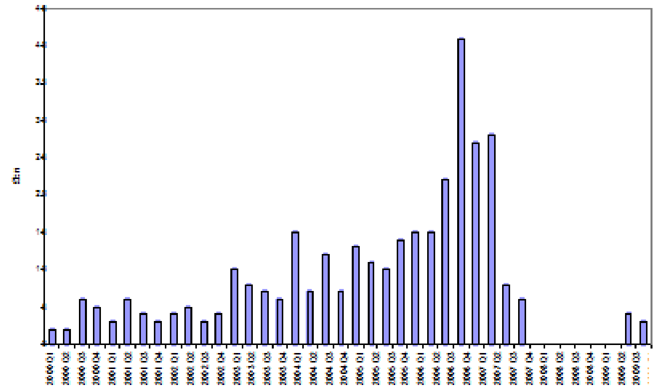
Based on the historical data, the Government of the United Kingdom has played a key role in ensuring a free and fair mortgage market in the country. This has improved efficiency and stability of the market compared to other European nations. A mortgage market with such characteristics provides better outcomes to consumers and firms. Similarly, it allows active participants in the market to make investments decisions with confidence. Basically, putting in place responsive and robust regulatory measures has been recognized as key elements in supporting growth of the mortgage market in the UK. This is because it builds the market by creating sustainability, innovativeness and as well, offers variety of products that meets needs of various borrowers. At the same time, the measures help in providing appropriate protection to consumers in the market. In the year 2004, the UK Government expanded the application of Financial Services Authority (FSA) regulatory measures by incorporating the first–charge residential mortgages. With respect to FSA regimes, it provides a number of important measures which include borrower protection, lenders must treat customers in a just and fair manner and any repossession must always be the last resort. In the same note, the FSA regime as well supports borrowers experiencing redress problems by offering the Financial Ombudsman Services (FOS). The consumer credit legislation contains regulations that govern other credit business such as second charge mortgage. The enforcement of the regulation is under the Office of Fair Tradition (OFT). The Consumer Credit Act 2006 implementation played an important role in strengthening the OFT regime. This act boosted the licensing regime by improving the OFT powers to access consumers and investigate complains to help in dispute resolution through FOS. Up to date, the UK government is still committed in maintaining a robust regulatory framework to support the mortgage market.

As opposed to this view, it was recently claimed that UK regulation in the banking sector has posed a serious constraints in the mortgage market. This means only few people in the country are capable of becoming home owners. Based on these comments it was projected that only one third of the total young generation in the UK could be home owners by the year 2020. This is approximately half of the total registered number in the year 1993 as contained in the report compiled by the IMLA (Intermediary Mortgage Lenders Association). Recent news showed that the European Union and the United Kingdom regulations are focused towards holding back the average lending volumes, as well as, prevent innovation in the mortgage market (BBC News, 2007a). With regards to the above scenario, it is recommended that a long term vision be established with regards to home ownership. The fallout resulting from the 2007/2008 financial crisis may have permanently downsized home ownership in the country. It was suggested in the report that the dramatic changes in the mortgage market after the economic downturn may perpetuate a fall in the home ownership unless proper regulation and market policy is put in place. Another highlight made with regards to the above scenario was that continued mortgage finance supply, FCA regulatory requirements and the new Basel III were the main barriers to proper recovery in the mortgage market. In addition to that, short term measures which include Help-to-Buy and Funding for Lending Scheme (FLS) were introduced to boost economic growth in the country. However, it was argued that the decisions on the above measures were reached without evaluating the long term purpose for establishing and efficient and stable mortgage market and private housing (Stolper, 2009). Therefore, the above scenario questions the nation's future as far as borrowers' ambition to home ownership is concerned; the recommended balance that will harmonize private rented markets and home owners and finally, the consequences of banking regulation to product innovation and lending volumes.

1.1.1 Wholesale Funding (1980-2007)

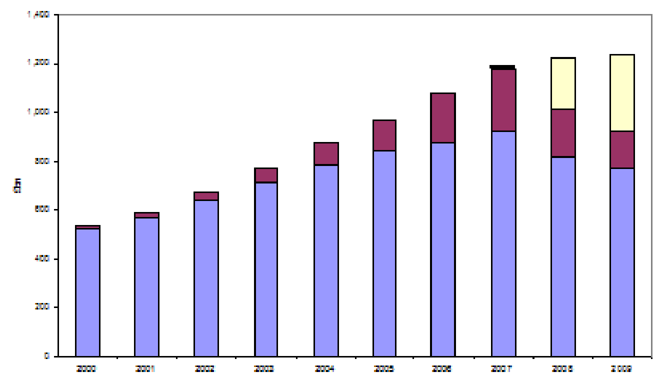
After the deregulation of the mortgage market in 1980s, wholesale funding was introduced as an important significant feature. This is because the system enabled specialist lenders and banks that were able to source wholesale funding to penetrate the market. However, by the end of 1990s, the significance of wholesale funding increased when large lenders in the mortgage market introduced the residential mortgage backed securities (RMBS) plan. Another development in the UK mortgage sector was realized in 2003 after the initiation of covered bonds (Council of Mortgage Lenders, 2010). This information is backed by Chart 1 below. The information in the Chart shows that the year 2000 was the period when large lenders changed to RMBS with regards to the total public issuance data. The peak point was reported in the year 2006 and 2007 as shown below.

Fig 1: Public Issuance of RMBS in the UK (Quarterly)



(Source: Council of Mortgage Lenders p6)

Fig 2: The funding of UK mortgage debt



(Source: Council of Mortgage Lenders p7)

The above graphs have clearly shown that the UK mortgage market has for over the years reported dramatic changed, most particularly during and after the credit crunch. In the present situation, first-time home, buyers in the United Kingdom must put in place a significant amount of deposits before being able to own property in the country. This trend continued irrespective of the falling house and property prices. Marcelo et al. (2008) stated that the pattern might not be familiar to anyone who acquired homes before the 1990s. The banking regulation trends posed enormous set back to the borrowers' expectations, especially, among those who sought to invest in low deposit and interest rate mortgages. The wider differences are because of the government, measures of the markets, and regulators. This essay, therefore, seeks to explain how the banking regulations impacted on the UK mortgage market.

1.2 Statement of the Problem

The main problem being realized currently in the mortgage market is the increasing interest rate and the amount of the required consumer deposits. This has narrowed the number of capable home owners in the United Kingdom. The main causes of this transformation include government regulatory measures in both the banking sector and the mortgage market. In the beginning, positive trends were noted till the year 2007 (peak year). The trend was reversed in the year 2008 onwards after the financial crisis hit. For this reason, it will help in examining various regulatory measures that the government put in place in the banking sector and how they impacted on the UK mortgage market.

The United States mortgage market is ranked the largest and has an open structure compared to other European nations. Report by Whitehead and Gaus (2007) noted that towards the end of 2006, the total amount of outstanding loans was approximated £3 trillion. This represented a 10 percent annual increase since the year 2000. In the year 2006, the proportion of mortgage debts to the overall GDP was approximately 83 percent making UK, the fourth largest after Switzerland, Netherland and Denmark. The value of housing asset in relation to the assets amounted to £3.5 trillion. This showed that the country was experiencing a high debt levels and a corresponding high debt repayments to income ratio.

In 2006, banks contributed to 60 percent of the gross lending with only 20 percent being offered by the building society. The country has over the years reported a rapid change on the range and mix of various mortgage products. In fact, the proportion of remortgaging loan was approximately 40% and a declining trend has been noted on the loan to value ratio. The standardized criteria lead to improved growth in the sub-prime lending. Most of these problems occurred as a result of deregulation. For this reason, the study seeks to analyze banking regulations and its impacts on the performance of the UK mortgage market.

1.3 Research Question

1. What are the main attributes of UK banking regulations and controls affecting the mortgage market**?**
2. What is the relationship between banks' deposit and interest rates on the demand of mortgage loans in the UK Mortgage market?
3. What are the major challenges faced by mortgage purchasers in the UK mortgage market?
4. Which bank is the best in terms of effectiveness in providing mortgage in the U.K?

1.4 Research Aim and Objectives

The main aim of this study is to investigate how banking regulation in the UK affected the performance of the mortgage market. The specific objectives to be addressed in the study include:

1. To investigate the main attributes of UK banking regulations and controls affecting the mortgage market**.**
2. To analyze the relationship between banks' interest rate and mortgage demand in the UK.
3. To analyze the major challenges of mortgage purchasers, house prices and the mortgage default rate in the UK mortgage market.
4. To determine the most effective bank that provides mortgage in the U.K

1.5 Rationale of the Study

The United Kingdom government has made significant regulatory changes in the Banking sector in the past few decades. These measures were aimed at creating an efficient and stable mortgage market, as well as, boosting economic growth in the country. The banking regulation established in the country has impacted significantly by transforming the performance of mortgage market. It is evident that current mortgage acquisition requires that borrowers increase their deposit base.

On average, not many individuals are capable of meeting the minimum deposit requirement, if perceived too higher. For this reason, it is important to study the impact of the government regulations by examining five main banking institutions in the UK. The outcome of this study may be relevant and useful to investors, banking institutions, and the general public.

1.6 Methodology

Given the scope of this paper, primary data collection may prove tiresome in this case. This is due to problems of time availability, geographical allocation and the willingness of the respondents to provide reliable information. For this reason, the study will focus on secondary data sources collected from journal articles, newspapers articles, online news source and books that discuss the main study topic. Data will be collected while focusing on five main banking namely Barclays, Santander Bank, Natwest Bank, Lloyds Bank and HSBC Bank. Reliable data addressing issues of UK mortgage market and trends in the house prices will also be used. The information collected will help in answering the main study questions.

1.7 Structure of the Dissertation

The dissertation will be organized into chapters as follows:

Chapter 1: Introduction-This chapter introduces the topic, give brief background of study, statement of the problem, research questions, and main research aims and objectives, rationale of the study, methodology and overall structure of the dissertation.

Chapter 2: Literature review: This section conducts a comprehensive review of previous studies that elaborates on the main study topic. Studies that relates to banking regulations and UK mortgage market

Chapter 3: Research Methodology-This chapter comprise of research philosophy, research design, research approach, research methods, research strategy, data collection methods, sampling method, and techniques of data analysis.

Chapter 4: Data Analysis, Presentation and Interpretation-In this chapter, the study will analyze the data (primary and secondary sources) and results presented in tables and graphical format. Interpretation of the results will be done under this chapter.

Chapter 5: Conclusion and Recommendations-This is the final sections in the dissertation that addresses the main research questions and as well, relates the outcome to the possible future implications. It draws conclusion and presents relevant recommendations that would enhance performance of mortgage market in the United Kingdom.

Chapter: 2 Literature Review

2.1 Introduction

Banking regulations and policies have significantly impacted on the performance of the UK mortgage market. Report by Council of Mortgage Lenders (2010) indicated that cost of acquiring houses and properties in the country have been increased in the past few decades at a fast rate. Based on the data that was recently produced by the Bank of England about the mortgage market, UK reported an increase in the net mortgage lending by GBP 6.5 billion in July 2005. This was the main reason behind the slowest growth rate registered in early 2000. The trends in the UK mortgage sector, especially, after the financial crisis hit showed signs of stability. The net lending in the market was at its lowest point in 2005 at an approximate value of GBP 6.5 billion. Currently, several views have been made on this topic that critically analyzes the trends in the UK mortgage market and its relationship with the banking regulation in the country. Among the areas of coverage in these studies include changes in house prices, the market volatility, lending requirements and repossession sub-primes and foreclosures rules. Based on this brief introduction, the next section will comprehensively review existing literatures addressing the above issues. This will help in assessing the underlining issues with regards to banking regulation and its influence on the UK mortgage market. I will examine issues regarding housing market, specific banking regulations and policies that lead to increase in lending costs, as well as, a rise in the housing prices. Given that mortgage market problem is a recent issue; I will focus on journals, newspapers and statistical data as the main source of information. A general information outlook and theories will help in understanding issues revolving the main study questions.

2.2 Definition of a Mortgage

A number of studies have different definitions for mortgages. Council of Mortgage Lenders (2010), states that a mortgage is a type of a loan that an individual uses to purchase a home. In this case, your home is used as the collateral. A legal contract is also signed as a surety that the person will repay the debt and other related cost and interest within the stipulated period that run between 15 and 30 years. In case of defaults, the lender has the right to repossess and sell off the property in order to recover the debt. Usually, repayment of the debt is done on monthly installments that comprise of the principal amount, taxes, interest and insurance (altogether denoted as PITI). Taylor (2008), referred to a mortgage as a written document which has both the mortgagor and the mortgagee. In such as scenario, the mortgagor is the home buyer (borrower) whereas the mortgagee is the bank or the lender- the institution lending money out to the home buyer. He further explained that the lending entity used the purchased estate as a security for the offered loan. Another definition by Thwaites and Wood (2003) states that a mortgage is a form of bank loan mainly designed, particularly, to buy a home. In a simple explanation, it is a type of a loan where the purchased property functions as the security. Usually, the lender caters for a greater percentage in the range of 80% of the total home price. This money has to be paid back with an interest within the specified period of time. In case the borrower fails to repay the loan, a foreclosure process is employed by the lender to recover the cost. Miles (2004) stated that a mortgage is a "home loan" or a "lien", - the amount of money home buyers owes on a real estate or property purchased. Mortgage is also referred to as a deed of trust or a legal document with a clear outlines spelling the agreement terms between the borrower and the lender. Finally, Miles (2004) describe a mortgage as "a loan to buy a home." It is similarly to other forms of loan in the sense that interest is charged on the principal amount. Monthly installment comprise of the principal amount plus interest among other payable charges.

2.3 Overview of the Mortgage in UK

As stated by Cameroon (2005), house prices in the UK experienced a boom that was mainly caused by volatility of the mortgage market. He further states that most mortgages offered in the UK are subjected to variable interest rates. In most cases, there is a higher rate of loan to value rates, as well as, a relatively easy re-mortgaging process. According to Cameroon, volatility in the market is caused by fluctuations in the interest rates, especially, on variable mortgages. As prices of houses increases, consumption among households and feeling of wealthiest also goes up and consequently, borrowers also have more collateral to help in getting more loans. This trend implies that rising house prices is observed by economists as a boost to good economic performance in the country. Kirchhoff and Block (2004) also claimed that house supply in the United Kingdom caused a remarkable transformation on the pricing. They argued that borrower's responsiveness to house supply trends declined over a period of time as the supply trend did not correspond to changes in price or demand. A mortgage market review in the study compared the situation of the 1980s boom to that of the early 2000. Based on the result, it was noted that between 1985 and 1988 period, there was a steady increase in the number of private household at the rate of 30 percent. The trend changed between the year 1999 and the year 2002 where an increase of 2 percent was reported. Therefore, the above scenario explains the significance of getting supply trends that corresponds to demand in order to keep price increase at a steady and recommended pace. The next section will cover some of the main components and characteristics of the UK mortgage market.

2.3.1 Legal Fee

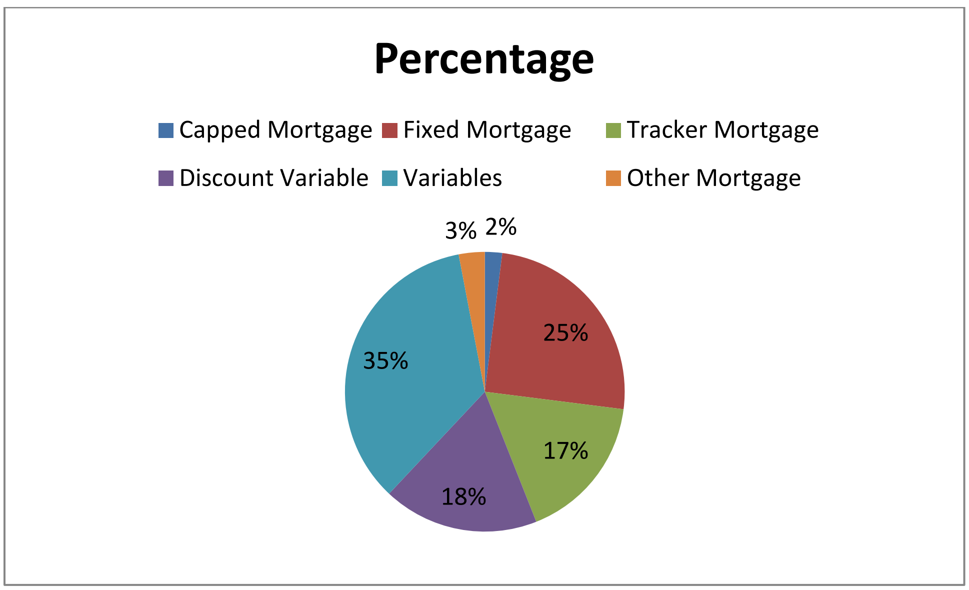
This is one of the fees chargeable in the process of acquiring a mortgage. Legal feel is one of the charges accrued to the borrower when applying for a mortgage loan. According to Chamberlin (2009), a legal fee is paid to the conveyance or solicitor who has been identified to represent the lender during the mortgaging process. As required by the rules, both the property buyer and the banking or lending institution must assign a solicitor to complete all the legal procedures on behalf of the client. In usual cases, lenders may provide the borrower with options regarding the legal process. The approximated legal cost incurred by the lender is in the range of £400. In most transaction, the lender expects the borrower to bear the legal costs.

2.3.2 Types of Mortgages in the UK

The flexibility created in the UK mortgage market resulted into development of several range of products. This enabled borrowers to choose among different mortgage alternatives. Consequently, it posed a great transformation on the face of housing market in the United

Kingdom. A rejoined by Thwaites and Wood (2003) showed that new mortgage types were introduced after lending regulations in the country were relaxed. They further stated that the introduction of more risky mortgage financing types contributed to a massive housing bubble in the country. Changes in the mortgage lending further allowed house owners to borrow with little collateral or no documentation that explicitly show income, employment and assets of the borrowers. Borrowers have an assumption that house prices would rapidly increase thus creating the possibility of selling home and making profit before repayment of principle commenced. Based on the above explanation, it was clear that UK mortgage market was largely characterized by variable mortgages rates. The types of mortgage offered explained the volatility status of the UK housing market. Mortgages in the UK are subdivided in the graph as follows:

Fig. 3: Mortgage Types in the United Kingdom



Source: (Miles, 2004, p6)

Miles (2004) summarized that the prevailing mortgage structure in the country made the UK market to depend heavily on the changes in the interest rates. This is opposed to the other countries with fixed rate mortgage system. The following are brief description of different types of mortgages as offered in the UK market.

2.3.2.1 Variable Rate Mortgage

As explained by Cameron (2005), a variable rate mortgage is a type where changes in the mortgage payments are largely dependent on the fluctuations reported in the interest rates. Basically, interest rates charges are attached to the base rate offered by the Bank of England. Alternatively, it can be fixed to other variable rates, for instance, the lender's standard variable rate (LSVR). The following are the main types of variable mortgages:

Tracker Mortgage: This is another type of mortgage offered within the UK mortgage market. Just like the variable mortgages, it also follows (Bank of England) BoE base rate, however, some certain percentage increase must be subjected to it. Tracker mortgages are offered to borrowers in different terms. In the views of Credit Choice (2010a), terms can either be the number of years or changed to LSVR (Lender's Standard Variable Rate) after the mortgage is completed. Credit Choice (2010a) further stated that lifetime trackers are available whereby instead of the specification of terms, the estimated margin on top of the existing base rate remains the same up to the time when the mortgage is completely recovered.

Discount Rate: This is another variable mortgage present in the UK mortgage market. The unique aspect of the discount mortgage is because of its attachment to the LSVR (Lender's Standard Variable Rate). As stated by Credit Choices (2010a), discount mortgages are not tied to the Bank of England's set base rates. Basically, approximately 70 percent of the mortgages present in the UK market are variables mortgages. One main problem that borrowers and other stakeholders noted in this mortgage type was that whether there is fluctuations in the Bank of England's rates, the monthly installments as well, changes.

2.3.2.2 Buy to Let Mortgage

According to studies by Ball (2006), Buy-to-let mortgage is a form that was designed, particularly, for the private investors who wants to buy properties and again let out to tenants. Ball pointed out that property is an important investment asset that can help consumers to earn more money through renting. It can also help consumers to achieve gains in capital with rise in house prices. According to statistic by Council of Mortgage Lenders (2010), the expansive growth in buy-to- let mortgage have reached an approximate number 991,600 and this translated to £116 billion by September 2007. Taylor (2008) on the other hand claimed that the growth in this market segment was in line with up-ward trends in real house price thus prompting speculations with regards to inflation in house prices. Reports further suggest that by the year 2000, the market of buy to let mortgages was at a steady rise whereby private investors buys properties purposely to immediately let them out to tenants. Basically, the UK has approximately 3.7 million residential of which one third were developed through buy-To-let mortgage process.

Fig. 4: The Number of Outstanding Buy-To-Let Mortgages (2000-2008)

Year	**Number of loans Outstanding (000)**	**Buy-to-let (proportion of the total mortgage market) (%)**
2000	120	1.1
2001	185	1.6
2002	276	2.4
2003	418	3.6
2004	526	4.6
2005	702	6
2006	850	7.1
2007	1026	8.7
2008	1156	9.9

Source (Mintel, 2009)

Based on the above table, it was evidenced that the buy-to-let mortgages reported an upward trend since the year 2000. However, the 2007/2008 financial crisis hit reversed the entire process. Mintel (2009) further stated that throughout the period, there was increase in the levels of new businesses. On the other hand, increased competition in the market also pushed up the loan to value ration and reduced interest rates to the level of standard mortgage rates. However, borrowers were confident in early 2000 that if the housing boom continues, the mortgage lending rates would be relaxed considerably.

2.3.2.3 Fixed Rate Mortgages

Fixed Rate Mortgage is a form of mortgage lending offered by banks in the United Kingdom. According to the information contained in the figure 3, the proportion of fixed rate mortgage lending in the UK was approximately 25 percent. This was a relatively smaller proportion compared to the Variable Mortgage Rate. Chamberlin (2009) stated that interest risks in FRM are assumed by the investors and creditors. On the other hand, Cameron (2005) stated that fixed rate mortgages exhibits a constant monthly repayment irrespective of the fluctuations in the market's interest rates. Recent reports also indicate that HSBC Bank provides range of fixed rate mortgages of 2 years, 3 years and 5 yeas repayment terms. In HSBC systems, the mortgages automatically revert to the Variable Rates after the end of the fixed period. Lambert (2013) in his part reported that a two year fixed rate mortgage is available to borrowers with 40% deposit at 1.5% rate whereas those with 25% deposit are given a slightly higher rate of 1.99%. In his further explanation, a five year fixed terms had slightly different conditions, in which, borrowers with 40 percent deposit paid 2.4 percent rates as opposed to borrowers with 25% deposits who were required to pay 2.84 percent rates. The following table gives detailed information of banks and their requirements on Fixed Rate Mortgages for bigger, middle and smaller deposit borrowers. Figure 8 to Figure 12 also give Fixed Rate Mortgages for Barclays, Natwest, Lloyd Bank, HSCB and Santander Bank.

Figure 5: Bigger Deposits

	Five Year Fixes		
Lenders	**Deposit (%)**	**Rate %**	**Fee (£)**
Tesco Bank	40	2.49	1495
N&P BS	35	2.59	200
Yorkshire Building Society	35	2.59	1475
HSBC	40	2.99	99
	Two Year Fixes		
Norwich & Peterborough	40	1.99	295
HSBC	40	1.49	1999
Post Office Mortgages	40	1.63	1995
Chelsea BS	35	1.64	1675
Chelsea BS	35	1.84	845
West Brom	25	1.99	994
Conventry Building Society	35	2.15	999

Lambert (2013)

Figure 6: Mid Range Deposits

	Five Year Fixes		
First Direct	25	3.19	495
Yorkshire Building Society	25	2.84	975
	Two Year Fixes		
Post Office Mortgages	25	1.98	995
Chelsea BS	25	1.99	1675
West Brom	25	1.99	994
Santander	-	2.84	995

Lambert (2013)

Figure 7: Smaller Deposits

		Two years	Five Year	
Lenders	**Deposit (%)**	**Rate %**	**Rate %**	**Fee £**
Clydesdale & Yorkshire Banks	20	3.19	3.79	
Hinckley and Rugby	20	-	3.45	890
First Direct	3.79	-	15	-
Chelsea BS	15	-	3.84	1675
Chelsea BS	4	-	4.54	375
Nottingham BS	10	-	4.39	299
Skipton BS	10	3.99		160
HSBC	10	3.59		999
Chelsea BS	10		3.54	1675

Lambert (2013)

Figure 8: Barclays Bank Fixed Mortgage Rates

Product	Initial interest rate	Follow on interest rate	The overall cost for compariso	Application fee	How much could I borrow?	Early repayment charge
10 Year Fixed	3.89%until 31 Dec '23	3.89%	4.1% APR	£1499	70%	3%
2 Year Fixed	2.8%until 31 Dec '15	3.89%	3.9% APR	£999	80%	3%
2 Year Fixed	1.99%until 31 Dec '15	3.89%	3.7% APR	£999	60%	3%
2 Year Fixed	2.18%until 31 Dec '15	3.89%	3.7% APR	£999	70%	3%
2 Year Fixed	2.35%until 31 Dec '15	3.89%	3.8% APR	£999	75%	3%
2 Year Fixed	1.89%until 31 Dec '15	3.89%	3.7% APR	£1999	65%	3%
2 Year Fixed	3.35%until 31 Dec '15	4.24%	4.2% APR	£499	85%	3%
2 Year Fixed	3.35%until 31 Dec '15	4.24%	4.2% APR	£999	85%	3%
2 Year Fixed	4.29%until 31 Dec '15	4.24%	4.3% APR	£0	90%	3%
2 Year Fixed	3.99%until 31 Dec '15	4.24%	4.4% APR	£999	90%	3%
2 Year Fixed Barclays loyalty mortgages	2.8%until 31 Dec '15	3.89%	3.8% APR	£499	80%	3%
2 Year Fixed Barclays loyalty mortgages	1.99%until 31 Dec '15	3.89%	3.7% APR	£499	60%	3%
2 Year Fixed Barclays loyalty mortgages	2.18%until 31 Dec '15	3.89%	3.7% APR	£499	70%	3%
2 Year Fixed Barclays loyalty mortgages	2.35%until 31 Dec '15	3.89%	3.7% APR	£499	75%	3%
2 Year Fixed Barclays loyalty mortgages** †	3.99%until 31 Dec '15	4.24%	4.3% APR	£499	90%	3%
2 Year Fixed Great Escape: Re-mortgage only	2.69%until 31 Dec '15	3.89%	3.8% APR	£0	70%	3%
2 Year Fixed Great Escape: Re-mortgage only	2.99%until 31 Dec '15	3.89%	3.8% APR	£0	70%	3%
2 Year Fixed GreatEscape: Re-mortgage only	3.74%until 31 Dec '15	3.89%	3.9% APR	£0	80%	3%

Source: http://www.barclays.co.uk/Mortgages/Fixedratemortgages/P1242557963470

Figure 8: Barclays Bank FMR

Product	Initial interest rate	Follow on interest rate	The overall cost for compariso	Application fee	How much could I borrow?	Early repayment charge
2 Year Fixed GreatEscape: Re-mortgage only	2.69%until 31 Dec '15	3.89%	3.7% APR	£0	60%	3%
2 Year Fixed Great Escape: Re-mortgage only	2.45%until 31 Dec '15	3.89%	3.7% APR	£0	60%	3%
2 Year Fixed Great Escape: Re-mortgage only	3.49% until 31 Dec '15	3.89%	3.9% APR	£0	80	3%
2 Year Fixed: Purchase only	2.69%until 31 Dec '15	3.89%	3.8% APR	£0	70%	3%
2 Year Fixed: Purchase only	3.49%until 31 Dec '15	3.89%	3.9% APR	£0	80%	3%
3 Year Fixed	2.4%until 31 Dec '16	3.89%	3.6% APR	£499	70%	3%
3 Year Fixed	3.24%until 31 Dec '16	3.89%	3.8% APR	£499	80%	3%
5 Year Fixed	3.59%until 31 Dec '18	3.89%	3.9% APR	£999	80%	3%
5 Year Fixed	2.99%	3.89%	3.7% APR	£999	70%	3%
5 Year Fixed	3.99%until 31 Dec '18	4.24%	4.1% APR	£999	85%	3%
5 Year Fixed	2.88%until 31 Dec '18	3.89%	3.6% APR	£999	60%	3%
5 Year Fixed	2.95%until 31 Dec '18	3.89%	3.6% APR	£1999	65%	3%
5 Year Fixed	4.89%until 31 Dec '18	4.24%	4.7% APR	£999	90%	3%
5 Year Fixed Barclays loyalty mortgages	3.59%until 31 dec '18	3.89%	3.9% APR	£499	80%	3%
5 Year Fixed Barclays loyalty mortgages	2.99%until 31 Dec '18	3.89%	3.6% APR	£499	70%	3%
5 Year Fixed Barclays loyalty mortgages	3.99%until 31 Dec '18	4.24%	4.0% APR	£499	85%	3%
5 Year Fixed Barclays loyalty mortgages	2.88%until 31 Dec '18	3.89%	3.6% APR	£499	60%	3%
5 Year Fixed Barclays loyalty mortgages	4.89%until 31 Dec '18	4.24%	4.6% APR	£499	90%	3%
5 Year Fixed GreatEscape: Re-mortgage only	3.99%until 31 Dec '18	3.89%	4.0% APR	£0	80%	3%
5 Year Fixed Great Escape: Re-mortgage only	3.29%until 31 Dec '18	3.89%	3.7% APR	£0	60%	3%
5 Year Fixed GreatEscape: Re-mortgage only	3.74%until 31 Dec '18	3.89%	3.9% APR	£0	80%	3%
5 Year Fixed, Great	3.09%until 31 Dec '18	3.89%	3.6% APR	£0	60%	3%
5 Year Fixed: Purchase only	2.99%until 31 Dec '18	3.89%	3.6% APR	£0	60%	3%
5 Year Fixed: Purchase only	3.74%until 31 Dec '18	3.89%	3.9% APR	£0	80%	3%

Source: http://www.barclays.co.uk/Mortgages/Fixedratemortgages/P1242557963470

Figure 9: NatWest Bank Fixed Mortgage Rates

Type	Initial Rate	Rate thereafter (Variable)	Overall cost for comparison	LTV	Product fee
2 year fixed rate	1.95%	4%	4.0% APR	60%	£1495
2 year fixed rate	2.69%	4%	3.9% APR	60%	£0
5 year fixed rate	3.05%	4%	3.9% APR	60%	£995
5 year fixed rate	3.35%	4%	3.9% APR	60%	£0
2 year fixed rate	2.99%	4%	4.0% APR	70%	£0
5 year fixed rate	3.45%	4%	3.9% APR	70%	£0
2 year fixed rate	2.18%	4%	3.9% APR	70%	£995
5 year fixed rate	3.35%	4%	4.0% APR	70%	£995
2 year fixed rate Shared Equity exclusive	3.15%	4%	4.0% APR	75%	£0
5 year fixed Shared Equity exclusive	3.59%	4%	4.0% APR	75%	£0
2 year fixed rate - Help to Buy	3.15%	4%	4.0% APR	75%	£0
5 year fixed rate - Help to Buy	3.59%	4%	4.0% APR	75%	£0
2 year fixed rate	3.70%	4%	4.1% APR	80%	£0
5 year fixed rate	4.09%	4%	4.2% APR	80%	£0
2 year fixed rate	3.15%	4%	4.1% APR	80%	£995
5 year fixed rate	3.79%	4%	4.1% APR	80%	£995
2 year fixed rate - FTB Exclusive	3.49%	4%	4.0% APR	80%	£0
5 year fixed rate - FTB Exclusive	3.89%	4%	4.1% APR	80%	£0
2 year fixed rate - FTB Exclusive	3.79%	4%	4.1% APR	85%	£0
5 year fixed rate - FTB Exclusive	4.49%	4%	4.4% APR	85%	£0
2 year fixed rate	3.35%	4%	4.1% APR	85%	£995
2 year fixed rate	4.39%	4%	4.2% APR	85%	£0
5 year fixed rate	4.69%	4%	4.5% APR	85%	£995
5 year fixed rate	4.89%	4%	4.5% APR	85%	£0
5 year fixed rate	5.05%	4%	4.7% APR	90%	£0
2 year fixed rate	4.89%	4%	4.3% APR	90%	£0
5 year fixed rate - FTB Exclusive	4.79%	4%	4.5% APR	90%	£0
2 year fixed rate	4.59%	4%	4.3% APR	90%	£995
5 year fixed rate	4.85%	4%	4.6% APR	90%	£995
2 year fixed rate - FTB Exclusive	4.49%	4%	4.2% APR	90%	£0
2 year fixed rate NewBuy Scheme	4.49%	4%	4.2% APR	95%	£0
5 year fixed rate NewBuy Scheme	4.79%	4%	4.5% APR	95%	£0

Source: http://www.natwest.com/personal/mortgages/mortgage-calculator.ashx?mode=view-fixed

Figure 10: Lloyd Banks U.K Fixed Mortgage Rates

Mortgage type	Interest Rate	End Date	Subsequent rate	APR	Max LTV
3 year Fixed Rate	3.34%	30-Nov-16	3.99%	3.90%	95%
3 year Fixed Rate	3.54%	30-Nov-16	3.99%	4.00%	95%
4 year Fixed Rate	4.19%	31-Jan-18	3.99%	4.20%	120%
4 year Fixed Rate	4.29%	31-Jan-18	3.99%	4.20%	120%
4 year Fixed Rate	4.39%	31-Jan-18	3.99%	4.30%	120%
2 year Fixed Rat	4.79%	30-Nov-15	2.50%	4.40%	120%
4 year Fixed Rate	4.84%	31-Jan-18	4.84%	5.00%	120%

Source: http://www.money.co.uk/mortgages/95-mortgages.htm

Figure 11: Santander Bank UK

Mortgage Type	Interest Rate	End Date	Subsequent Rate	APR	Max LVT
2 year fixed Rate	1.89%	2-Dec-15	4.74%	4.40%	65%
2 year fixed Rate	1.89%	2-Dec-15	4.74%	4.40%	60%
2 year fixed rate	1.89%	2-Dec-15	4.74%	4.40%	60%
3 yaer fixed rate	1.99%	2-Dec-16	4.74%	4.40%	70%
3 year fixed Rate	1.99%	2-Dec-16	4.74%	4.20%	70%
3 year fixed rate	1.99%	2-Dec-16	4.74%	4.20%	70%
2 year fixed rate	1.99%	2-Dec-15	4.74%	4.40%	60%
2 year fixed rate	1.99%	2-Dec-15	4.74%	4.30%	60%

Source: http://www.money.co.uk/mortgages/95-mortgages.htm

Figure 12: HSBC Bank UK

	Interest Rate	End Date	Subsequent Rate	APR	Max LVT
2 year fixed Rate	1.49%	31-Jan-16	3.94%	3.70%	60%
2 year fixed Rate	2.19%	31-Jan-16	3.94%	3.80%	70%
2 yaer fixed rate	2.19%	31-Jan-16	3.94%	3.70%	70%
2 yaer fixed rate	2.19%	31-Jan-16	3.94%	3.80%	70%
2 year fixed Rate	2.39%	31-Jan-16	3.94%	3.80%	60%
2 year fixed rate	2.49%	31-Jan-16	3.94%	3.80%	70%
5 year fixed rate	2.99%	31-Jan-19	3.94%	3.70%	70%
5 year fixed rate	2.99%	31-Jan-19	3.94%	3.70%	70%
5 year fixed rate	2.99%	31-Jan-19	3.94%	3.70%	70%
2 year fixed rate	3.09%	31-Jan-16	3.94%	3.90%	80%
2 year fixed Rate	3.09%	31-Jan-16	3.94%	3.90%	80%
2 year fixed Rate	1.49%	31-Jan-16	3.94%	3.70%	60%

Source: http://www.money.co.uk/mortgages/95-mortgages.htm

2.3.3 Credit Facilities in the UK mortgage market

It is perceived by many that the conditions for credit facilities amongst borrowers in the United Kingdom since the year 1970s have been liberalized. Goodhart et al (2004) pointed out that there are two main principal agencies that contributed to 1980s economic boom the 1990s global recession. These include the consumer spending (consumption) and the mortgage (housing market). Changes noted, particularly, with regards to the availability of credit facilities may have played an important role with regards to retrenched consumption, as well as, house price booms. By the year 1980s, most countries completely eliminated restrictions on credit market- deposits and interest ceilings. They also failed to control movements of international capital across borders. Mintel (2009) explained the need to establish a credit condition index (CCI) to help in measuring credit availability. Basically, credit facilities availability in the UK has been governed by a number of factors namely government regulation of the banking institutions and the corresponding regulation of the mortgage market within the country. Borrowers in the UK can access credit facilities from renowned financial institutions, as well as, building societies and securities firms. The following table gives details of the top ten leading mortgage lenders in the sector, the average mortgage asset value and the percentage assets accrued to the company.

Fig 13: Mortgage Asset Value and the Percentage Assets of the Lender

Rank	Name	Mortgage asset value	%assets of the lenders
1	Lloyds Banking Group	350.5	35%
2	Santander	159.2	16%
3	Nationwide BS	136	13%
4	Barclays	82.2	8%
5	Royal Bank of Scotland	76.6	8%
6	Northern Rock	66.7	7%
7	HSBC Bank	50.5	5%
8	Bradford& Bingley	41	4%
9	Bank of Ireland	27	3%
10	Britannia BS	22.1	2%

Mintel (2009)

2.3.4 Banking Regulations

As was pointed out by Goodhart et al. (2004), the main cause of the financial crisis hit was the failure on the side of financial institution with respected to putting in place an effective regulatory mechanism. Self regulation through the use of banking codes, as well, did not prevent the banking crisis that occurred in 2007/ 2008 period. In fact, high risk trading involving the use of complex products in the financial market, options and derivatives alongside increased assets securitization resulted into a shadow banking system- A practice that is beyond the normal banking system. Just like any other large business enterprise, banking institutions are regulated by the Competition Commission (CC) and OFT. Garratt and Pannell (2001) stated that by the year 2001, large banking institution in the UK were operating under a complex monopoly, especially, when providing services to (SMEs) small and medium sized enterprises. According to the report, this reduced the competition level in the market thus detrimental to the borrowers and consumers. For instance, customers found it difficult to switch from one bank to the other since products and services offered by the banking institutions were similar.

2.3.4.1 The Tri-Partite System

Examining the current banking regulations being undertaken in the United Kingdom, it involves participation of three main organizations. These include the Bank of England, The treasury and the renowned Financial Service Authority (FSA). As was pointed out by Garratt and Pannell (2001), during the period prior to the banking crisis, banking regulations in the country was referred as a light touch meaning that, there was no aggressive regulatory engagement by key regulators. Actually, they mainly came in limited scenarios, especially, when necessity arises. Regulators actions was based on the fact that if heavy touch regulation was established, there was high probability that multinational financial cooperation would invest heavily in countries with limited regulations. This implies that they will vacate London therefore, creating high level of unemployment in the City.

2.3.4.2 FSA Role

As an important participant in the UK banking regulation, Financial Service Authority is ranked the main regulator within the UK banking sector. According to Goodhart et al (2004), FSA has two main goals to achieve: (1).To promotes fairness and efficiency in the UK financial service sector and (2). To assist consumers in the financial service sector in achieving fair and valuable deals. As part of the organization's strategy to meet these objectives, FSA developed standards that must be met by financial businesses and other banking institutions which must be met considerably.

2.3.4.3 Principles and Rules

In the views of some critics, the regulatory system in the US is mainly based on rules. Therefore, people have the view that it should be transformed into a system based on principles as in the case of European model. Chrystal and Mizen (2005) stated that rule-based regulations is a system where regulators follows and interpret stipulated rules as contained in the law. This means that a very limited space is left for interpretation and judgments. Alternatively, they claimed that principles based system is somehow flexible and follows general principles that are within the legislations thus giving regulators opportunity to assess and monitors activities and behaviors of lenders and other financial institutions.

2.3.4.4. The UK Banking Act of 2009

As contained in the Chamberlin (2009), the banking Act 2009, was established with the main objective of maintaining stability and protecting depositors in the country. The Act of 2009 was designed to help regulators by enabling them have a collective power to avert crisis that may arise in the banking system. For instance, they were given the powers to subject any failing bank under a temporary ownership by the public. A review was made by Lord Turner in 2009 who was by then the Chairman of the Financial Service Authority. Based on his reviews and findings with respect to the banking crisis, he provided a number of recommendations that needs to be focused on. He suggested the establishment of a well coordinated banking regulations with the international community, more specifically, the developments of a pan- European regulators. Other recommendations includes: Banks holding more asset base, liquidity regulations, more information on hedge funds and other related activities to be collected from banks that practices the shadow banking system, host countries to regulate overseas banks, controlling employees remuneration within the banks and a comprehensive reviews of accounting practices within the banks.

2.3.5 Interest Rate Policy

The most recent interest rate benchmark that Bank of England reported in the U.K was approximately 0.5 percent. Houseweb (2009) data indicated that between 1971 and 2013, the UK had an average Interest Rate of 8.19 percent. The highest percentage was reported in July 1980 at an approximately 17 percent. The lowest value recorded was in March 2009 at 0.5%. Substantially, the Bank of England in the UK operates independently. All decisions with regards to interest rates are made by the MPC (Monetary Policy Committee). The official interest rate set by the Bank of England is known as the repo rate. The repo rate once set must be observed by other counterparties and Bank of England when undertaking open market operations. Among the counterparties groups includes securities firms, building societies and banks. The following table summarizes interest rates between 1990 and 2009.

Fig 6: The United Kingdome Interest Rates (1990-2009)

Year	Rates %
2009	0.5%
2008	2.0%
2007	5.5%
2006	5.0%
2005	4.5%
2004	4.8%
2003	3.8%
2001	4.0%
2000	6.0%
1999	5.5%
1998	6.3%
1997	7.3%
1996	6.0%
1995	6.5%
1994	6.3%
1993	5.5%
1992	7.0%
1991	10.5%
1990	14.0%

Source: (Houseweb, 2009)

Based on the information presented in the table, Houseweb (2009) evidenced that interest rates have been declined in the UK since 1990s. This made borrowers to acquire more mortgages since worries on mortgage repayments were eliminated. Though house prices have been going up and the declining interest rates made houses affordable to many people in the UK.

2.4 Major Determinants of House Prices

A study by Aoki (2001) indicated that both demand and supply factors significantly influenced house price in the United Kingdom. They were the main factors that when combined together led to the housing bubbles in the country. The next section will briefly explain the above factors and their influence on house prices.

2.4.1 The Demand Factor

Theoretically, an increase in houses demands results into an increase in prices. Thwaites and Wood (2003) examined the boom years and noted a number of factors that influenced houses demands. Among them includes interest rates, real income or economic growth, unemployment, speculations, demographic factors, mortgage finance availability and the consumer confidence.

2.4.1.1 Income

As an important factor, Aoki (2001), claimed incomes of potential borrowers helped determine house prices. For instance, if people have more disposable income, they are more likely to go for a mortgage loan and purchase houses. GDP data is applicable when measuring household income. The following graph shows the relationship between the GDP and house price in the UK.

Fig 7: The GDP and House Prices Correlation in the UK

Source: (Aoki, 2001, p 462)

According to the information presented in the graph, it was clear that a correlation exists between a change in GDP and changes in house prices. With this kind of relation, it is viable to conclude that when income goes up, borrowers are likely to buy more houses thus elevating houses demand.

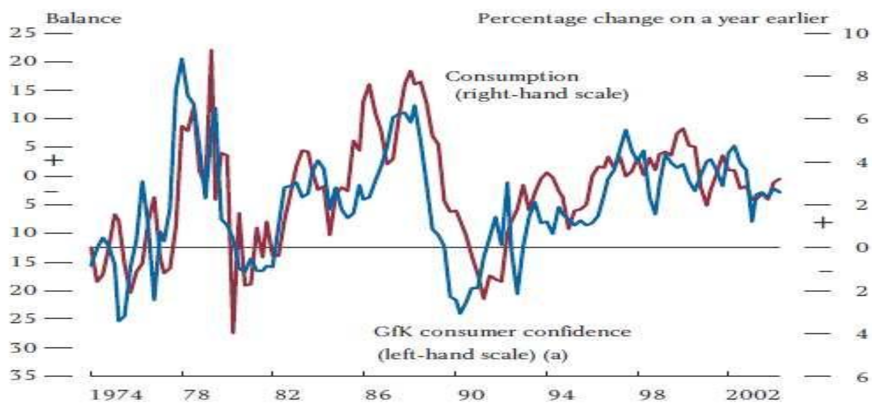
2.4.1.2 Interest Rate

This is another factor that determined house prices in the UK. Depending on the levels of interest charges, it influenced the willingness of potential borrowers to acquire mortgage loans. At low interest rates, there is high likelihood that people would take mortgage loans. The opposite happens during periods of high interest rates. Statistical data showed at figure 6 which is falling trend in interest rates between 1990 and 2009 and this explains the rise in mortgages number within the UK mortgage market during the same period.

2.4.1.3 Consumer Confidence

This is another factor that determines house price. Consumer confidence is measured in order to understand the relation between growth in household consumption and the confidence. Berry (2004) analysis focused on the influence of consumer confidence to the performance of the general market. This was accomplished by examining the correlation between consumption levels and consumer confidences. The Graph below illustrates the relationship between consumption and consumer confidence

Fig 8: Relationship between Consumer Confidences and Consumption Rate



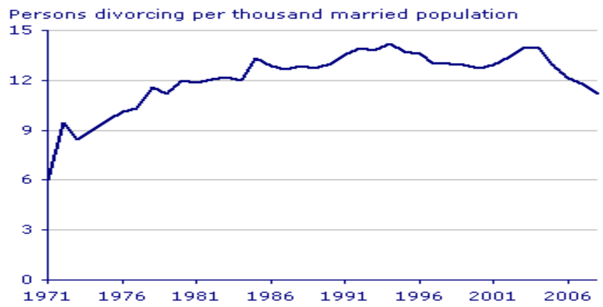
Source: (Berry, 2004, p282)

Based on the information presented in the table above, confidence movement in the UK portrayed a close association with the trend in the real annual consumption levels for a period of 30 years. The information is very usefully, particularly, when examining the consumer confidence and its effects on house prices. Practically, consumer confidence determines price of houses in the market. Berry (2004) claimed that high consumer confidence makes them hope that the market performance will continue to increase and this consequently creates the willingness to acquire riskier mortgages. This explains high mortgage loans reported in early 2000.

2.4.1.4 Demographic Factors

Research further states that demographic factors play an important role by affect houses demand. Among them include increased immigration, high divorce rates, increased life expectancy and fewer marriages. Office for National Statistics (2010a) showed that since 1970s, UK had reported an increased level of divorce rate. Based on the information presented in the following graph, the divorce rate in the UK by early 2000 had significantly increased.

Fig 9: The Divorce Rate: England and Wales (1971-2006)



Source: (Office for National Statistics, 2010a)

The table above indicates that in early 2000s, there were high divorce rates in the country therefore, explaining the corresponding increase in houses demands. When divorce rate goes up, large number of people is in search for alternative accommodation after separating from their partners.

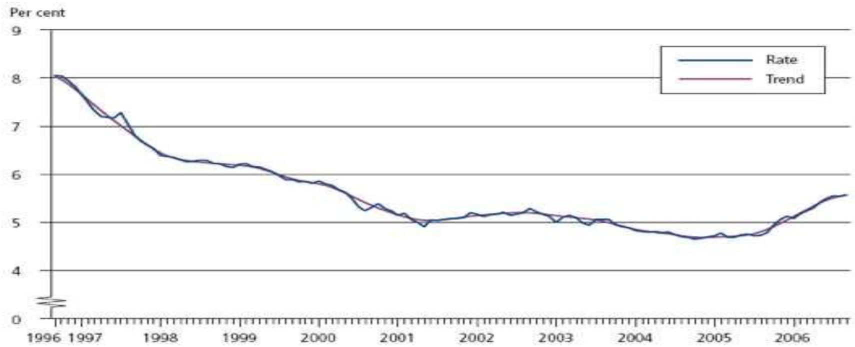
2.4.1.5 Speculations

This is another factor determining house prices. Greater percentage of properties offered in the UK mortgage market was under the buy-to-let mortgage. This was a clear indication that most investors in the mortgage market aims at obtaining income or gaining more capital from their investments. Therefore, most investors will purchase houses during periods of price increase and dispose them when market turns thus increasing market volatility.

2.4.1.6 Unemployment

As an important factor, low level of unemployment is correlated to an increase in houses demands. Period of low unemployment means that many people have jobs and can afford to take mortgage loans and purchase houses. The following graph explains the relationship.

Fig 10: The Unemployment Rate in the UK (1996-2006)



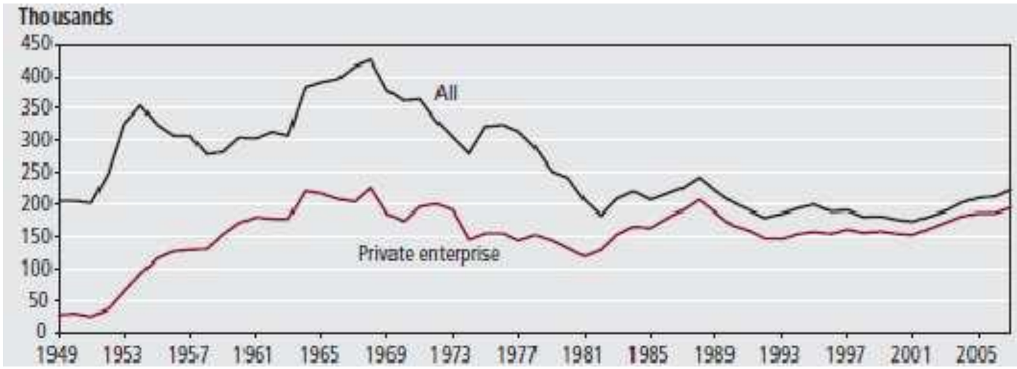
Source: (Goodridge, 2006, p.401)

The information in the graph above indicates that since the year 1996, the UK has reported a steady decline in the Unemployment rate. The figures were high at 8 percent and declined to 5 percent in the year 2000. In periods of housing boom, there was a very low unemployment rates which also affected the overall housing demand.

2.4.2 Supply Factor

Constitutively, Credit Choices (2010a) stated that short time supply factor have limited effects on house price since building of houses takes a long time. For this reason, it is possible to say that the market is experiencing shortage in house supply as the supply cannot meet the growing demands in the market. Long term supply factors that determines house prices are also very few. Among them include subsidies, legislations, costs and resource availability. The supply is also influenced by the existing number of house sellers at a given period of time. The United Kingdom is a small country with an averagely condensed population and this makes it difficult to get space to put up new buildings in order to meet the growing demands in the market. In this case, cost of building may go up and consequently, pushing the house prices up. Alternatively, Taylor (2008) stated that government legislations may interfere with housing supply in the market. Strict planning requirements must be established when putting up new buildings. This affects the entire building process. If government offers subsidies to those building house, it can significantly boost supply in the market and influence house prices.

Fig 11. The Completed Permanent Dwellings in the UK (1945-2005)



(Source: Chamberlin, 2009, p.36)

The graph above shows the average permanent dwellings that were completed in the United Kingdom between 1945 and 2005. According to Chamberlin (2009), though there was an indication that the number of completed buildings went up in 2001, it was relatively slow compared to the previous historical performance. Complex planning system may be the cause of poor price signals and housing supply in the country. Given the fact that house building takes a longer duration, it favors mainly the large corporations with huge resources to sustain their operations. This has reduced competition in the market and significantly influenced house prices.

2.5 Bank Credit Facilities

Banking institutions in the UK offers variety of credit facilities. Stolper (2009) pointed that credit facility is organized by companies through closing of equity financing. In this approach, companies are able to raise funds through selling of shares. One of the key issues that companies must take into consideration is the incorporation of debts within the capital structure. In addition, companies should also examine parameters surrounding equity financing. Banking institutions, building societies, as well as, security firms provides wider range of financing solutions to personal and commercial clients. Among the financial needs supported include financing account receivable, project planning, hire purchase, mortgage financing, private equity funds, overdrafts and personal loans. Cross-border financial solution is also offered by most financial institutions.

2.6 Major Challenges of Mortgage

There are a number of challenges that have affected mortgage financing. Garratt and Pannell (2001) claimed that the greatest challenges includes high pricing, increased costs and general market volatility. In the current market place, even borrowers with clean credit history are facing difficulties, particularly, with regards to obtaining mortgage funding. They further explained the following as the key challenges affecting the mortgage market.

2.6.1 Liquidity Crisis

The financial crisis hit affected the lending capabilities of most financial institutions in the United Kingdom. This has made the mortgage market to be less attractive because of restricted lending and fewer buyers. Based on this scenario, most lenders do not have adequate resources to facilitate the market and at the same time, buyers lack essential equipments for their mortgage loan to be approved.

2.6.2 Banks Financial Condition

This is another challenge that affected mortgage financing. Difficult economic conditions have affected liquidity status of financial and banking institutions. In facts, funds availability keeps fluctuating and the market place is experiencing endless uncertainties.

2.6.3 Evaluation

The criteria of evaluating and approving mortgage loans in the UK are relatively complex. Lenders only focus on investors with enough income and security depositors to have the surety that they will recover the loan. Lenders hesitate, especially, if the borrower is bankrupt or has a bad credit history.

2.6.4 Property Dispute

Another challenge is case of dispute in collateral property. This may arise in case of problems of ownership or legal problems. In such a situation, lenders may not implement mortgage financing for the borrower. Basically, both the lender and mortgage insurer must agree before transactions are completed.

2.7 Advantages and Disadvantages of Mortgages

As an important financing source, mortgage market exhibits a number of advantages and disadvantages. Council of Mortgage Lenders (2010) stated that as a long term investment, mortgage loans posses both negative and positive sides as presented as follows:

2.7.1 Advantages

2.7.1.1 Achieve Home Ownership

Through mortgage loans, one is able to purchase homes through installments without full price payments. However, the investor is required to pay deposit of about 20% of the total buying price. Through mortgage loans, the borrower has free income available for other projects.

2.7.1 2 Investors Have Access to Cash Flow

Home equity loans are not used in buying a home therefore, enables allows borrower to access money whenever they need. Such many can be used for college tuition, medical bills and home improvements or repairs.

2.7.1.3 It Improves Credit Rating of Borrowers

Mortgage loans can be used by investors to improve their overall credit scores. Individual credit score is important in determining interest chargeable on credit products- credit card and car loan. If the borrower has a history of on time repayment of mortgages, it improves the overall credit rating and lenders can use it as a benchmark to extend more credit facilities.

2.7.1.4 Tax Benefit

Investors with mortgage loans enjoy tax reduction. This further reduces the borrower’s tax liability. Any interest payable on mortgage is tax deductible. On the other hand, mortgage and homeowners insurance can also cause a tax reduction on investors.

2.7.2 Disadvantages

2.7.2.1 Loss of Collateral

In mortgage loans, the purchased property acts as a security. The lender uses it as a guarantee that the awarded loan will be recovered. In case the investor or borrower fails to repay the loan, the lender has the right to take over the house and the borrower loses all the money paid prior to the default.

2.7.2.2 Asset Depreciation

This is another negative aspect of mortgage loans. The home purchased depreciate in value with time. As repayment is made, the home value is subjected to several factors some of which are beyond the control of borrowers. It should be noted that the mortgage value remains constant as the purchased house loses its value. This means that the investor made end up having a loan balance greater than the home value.

2.7.2.3 Types of Mortgage and Obligation Risks

As pointed out by Chrystal and Mizen (2005), there are various forms mortgage loans and its acquisition follows a complex procedure. For this reason, the borrower may not understand fully the implications of the chosen loan options. For instance, a fixed rate mortgages are subjected to the same rate of interest throughout the repayment period leading to higher payments being made. Alternatively, adjustable rate mortgages are the most attractive form because of lower rate of initial interest. Higher payments only come when there is the reset. On the other hand, mortgage loans that posse's balloon rider is usually followed by a large lump sum payments being made at the end. Investors who are not able to off-set the lump sum cannot be awarded new loans and their property can be reposed by the lenders.

2.8 Conclusion

In summary, the above literature review is comprehensive in the sense that several studies, mainly journal articles and newspapers have been utilized. In these sources, they have tried to analyze the prevailing situation in the mortgage market and banking regulations. The main areas covered in the studies include issues such as the housing market structure, trends in house prices, banking regulations, credit facilities, mortgage facilities and its advantages. The review clearly indicates that banking regulations and volatility of the market have greatly affected the performance of the UK mortgage market. The next chapter covers the research methodology.

Chapter 3: Research Methodology

3.1 Introduction

This chapter is aimed at evaluating various methods of research that were employed in the study. In the same note, the section also explains methods that were used in data gathering, as well as, data analysis. Besides, provides the reader with adequate information with regards to procedures and process undertaken when conducting the research study.

3.2 Research Philosophy

As an important component of research methodology, research philosophy is an important component of the methodology because it enables the researcher to identify and follow the best approach that would enhance collection of proper and effective data. In this respect, Johnson and Christensen (2010) had the view that research philosophy and paradigm is largely dependent on a number of shared practices, concepts, values and assumptions. Among the applicable philosophies include positivism, realism and interpretive philosophy. However, positivist believes that truth about a phenomenon is in the field and can be collected by use of research instruments, measured and analyzed through the use of statistical tools (Bryman and Bell, 2003).

According to Johnson and Christensen (2010), the interpretive philosophy states that social world of business and management is very complex beyond the formulated laws and theories as opposed to the case of natural science. In this model, maximum truth and lots of meaning is contained in simple facts thus critical in solving key research problems. The above philosophy was identified because of its significant role in producing an effective end results.

3.3 Research design

In this study, regression and exploratory methods were employed in order to understand the UK banking regulations and how it affected the performance of the mortgage market in the country (Creswell, 2003). The research also incorporated the quantitative and qualitative methods so that precision of the outcome can be improved. This being the case, the research is aimed at collecting, analyzing and summarizing the existing literatures with respect to banking regulations, trends in the mortgage market, house prices, mortgage lending situation and the overall outcome in a situation where all the factors are combined. The paper is mainly concerned with examining the relationship between banking regulations and performance of the UK mortgage market. Furthermore, UK mortgage market and its related activities have been widely discussed in various media, most particularly, the prevailing house prices, the housing bubbles, the trends in the markets and the lenders behavior (Saunders 2009).

3.4 Research Approach

There are two main research approaches that were utilized in this study. These include the deductive and inductive approaches. The main difference between the two is the approach being applied. Alternatively, the decision undertaken in choosing an appropriate approach is also based on the ability to effectively answer the main study questions. Saunders (2009) stated that inductive approach emphasizes on social meaning and how investigator and the topic relates. This is different from deductive approach that relies heavily on analysis and measurements of variables. In addition, the deductive reasoning can be summarized into three main stages namely theory development, hypotheses formulation and hypotheses testing (Ticehurst and Veal, 2005). This study emphasized on the two approaches in order to effectively understand the relationships between the variables.

3.5 Research Methods

In most studies, a mixed research methods have been employed- combining the use of both quantitative and qualitative research. Creswell (2003) argued that the use of the two methods in a concurrent manner provides a better meaning to the key research problems. By using the two methods, it capitalizes on their strength while compensating the possible weaknesses associated with the methods. In this research, quantitative method was given dominance but also used open-ended questions for mortgage specialist who works in the banks. Primary data was collected using questionnaire and analyzed using both single and multiple linear regression models.

3.6 Research Strategy

Data was collected from both primary and secondary sources. Primary data can be collected using questionnaire surveys and interviews. On the other hand, secondary data can be obtained from peer reviewed literatures. There also some other components of social research methods applicable in this scenario such as laboratory and field experiments, case studies, simulation, forecasting and theorem proof. However, as was stated earlier in the paper, this study mainly emphasized on the primary data sources that were collected from participants of survey questionnaire and interviews of mortgage specialists. The use of secondary data was arrived at because of the associated advantages. Among these benefits include presence of high quality secondary data, ethicality and time saving. Through the use of secondary data, it provides the opportunity to cover a wider information selection, as well as, give an opportunity to perform a comprehensive conclusion. On the other hand, collecting statistical data necessary for this study using survey tools was as well, difficult compared to the use of secondary data. The model employed was theory based with emphasis being put on other peoples' ideas incorporated by personal developments of the researcher (Sekaran, 2006).

3.7 Data Collection Methods

In the literature review section, the method of collecting secondary data were also employed mainly retrieving online secondary sources. Among these sources include books, newspaper articles, journal articles and websites sources. Information on the following banks was also used: - Barclays bank, Lloyd banking group, Natwest Bank, Santander Bank and HSBC bank. Secondary data was important in understanding key study areas. In the literature review section, historical data on banking regulation, trends in house prices and general performance of the mortgage market in the UK were incorporated in the study. However, emphasis was placed on primary data collection using questionnaires survey tool with interview questions. Random sampling was done when identifying the most appropriate organization and respondents to help in answering study questions. Independent and dependent variables were identified to facilitate the regression model.

3.7.1 Regression Model

This model was used because it helps to predict the relationship between one variable and other variables. It is a model that supports scientific research through the provision of a powerful analysis tool thus, enabling the prediction of events. The model of regression for this study was employed because it saves time and money. On the other hand, it helps in collecting information and predicting its position in future times (Sekaran, 2010). For this reason, it will be important to construct a workable regression models using the identified variables. The information needed was obtained from the selected banking institutions and other source. This was followed by modeling the information in a linear transformation. Before the construction of the model, information on the variables was initially collected using a questionnaire tool. The variables to be analyzed include mortgage demand, interest rates, house prices and mortgage default rates amongst others. The following is a notation for the applicable regression model.

X_i = Independent variables (demand of mortgage loans, Mortgage financing, mortgage default rate, performance of mortgage market)

Y_i = Dependent variable (Performance of real estates, Interest rates, bank deposit, house prices, banking regulations)

Y'_i= Values predicted for the dependent variable

3.7.2 Organization Background

In this section, the study will present brief profiles of the selected banking institutions identified to play an active role in the UK mortgage market. Most of these selected banks operate internationally. The five main banks to be used in this study include: HSBC Holding, Barclays Bank, Lloyds, Natwest Bank and Santander Bank. The brief profile is as follows:

3.7.2.1 HSBC Holding Plc

This is ranked among the largest banking institutions worldwide. It is estimated to offer service to approximately 95 million customers. This was achieved through establishment of a robust international network comprising of over 7500 offices distributed in over 888 stations. Regionally, HSBC Holding operates in Europe, Middle East, Asia, Africa, South America and North America. In 2010 December, HSBC was ranked the largest listed company within the LSE (London Stock Exchange Market). The market capitalization of the company was estimated at $180 billion. The company opened its business doors in Hong Kong in March 1865 and serves about 58 million customers in over 80 territories and countries. The past 148 years experiences have created the HSBC character, the organization believes in capital strength, building long term relations with customers, and strict cost control (Latter 209). HSBC has constituted to change in all forms including new technologies, economic crises, and revolutions. In this case, it has adapted to survive with the resulting corporate character of the organization enabling it to deal with challenges of the modern world. Currently, HSBC is reported to be the most liquid and capitalized bank in the world. It has 12.1% tier one capital ratio and an approximately 78.1 percent of (loan: deposit) ratio. Total assets of the company were estimated at US$2.455 trillion, as well as, a pre-tax profit amounting to US$19.04 billion.

3.7.1.2 Lloyds Banking Group

This is ranked the fourth largest banking institution in the United Kingdom. It is the leading provider of mortgages, credit cards, personal loans, savings and current accounts in the UK. They are estimated to serve approximately 30 million clients and total number of employees in the range of 104,000 people. The main brands for the Group include Gloucester, Cheltenham, Halifax, Bank of Scotland, Scottish Widows and the Lloyds TSB. Main brands selling in Wales and England include Halifax and Lloyds TSB. It is classified as the largest retail service provider in the UK. It is also the third largest in the provision of general insurance. They have a total asset base amounting to GBP 966.770 billion. The TSB Foundations of Lloyd's comprised of four autonomous grant-making trusts that covered Scotland, England and Wales, Channel Islands, and Northern Ireland. Lloyds is a market within which underwriters from independent underwriters of insurance join to sell insurance under the name Lloyd's (Devine and Jenny 26). It began it operation in the 17th century with ship owners and merchants who joined together in order to share risks. The company is presently a globe's leader in the insurance market. Its initial name was Lloyds of London that changed in 1997and became Lloyd's.

3.7.1.3 Natwest Bank

Natwest Bank was formed in 1968 through merger between the National Provincial Bank and Westminster Bank. It is part of the Royal Bank of Scotland and operates as a wholly owned subsidiary. The merger enhanced the strength of the balance sheet establishing chances of streamlining the branch networks and facilitated greater investment in new technology. The legal integration procedure ended in 1969, and trading began in January 1970 (Burke, p.156). It offers services such as credit cards, access, computer-related cash dispensers, service tills, telephone banking, touch-screen share dealing. Currently, the Bank is part of the globe's groups of financial service. According to the 2012 statistic, Natwest Bank is ranked among the largest commercial and retail banking institution. They serve a total of 12 millions clients and a total asset base worth £374.33 billion. It is one of the four largest clearing banks with approximately 1600 branches in UK and 250 branches within Ireland. December 2012 data shows that customer accounts were worth £267.224 billion whereas loans and advances amounted to £137.260 billion.

3.7.1.4 Barclays Bank

Barclays bank is classified among the global financial services group. It is a British financial services and multinational banking company based in London, U.K. The bank operates in America, Europe, Asia and Africa region. The bank presence is found in 50 countries and a global customer base of approximately 50 million. It is the second largest banking institutions in the UK market with regards to asset base. The average total asset base is estimated at £1,564 billion. Being a universal bank, it carries operations in investment banking, retail, and wholesale. It also carries out mortgage lending and credit cards, and wealth management and operates in more than 50 countries. It has about 48 million customers. The company is organized within Investment and Corporate Banking. Its origins are traced in a banking business known as Goldsmith developed in 1690, in the city of London. In 1736, James Barclay became a partner in the business, and the name Barclays was created in 1896. It has a primary listing in the London Stock Exchange and is a constituent of the FTSE 100 Index (Monteith p, 15).

3.7.1.5. Santander Bank Plc

This is one of the leading banks in the United Kingdom that offers personal financial services. It also plays a key role in the savings and mortgage businesses in the country. Santander

Bank Plc is ranked the largest within the Eurozone region with regards to market capitalization. The bank originated from Spain and has in the recent years expanded through acquisitions and established operations in Asia, North America, Latin America and Europe. Most of the subsidiaries of the company in other parts of the world have been rebranded and given the Santander name. June 2013 report shows that the company had an operating income amounted to £990 million and profit before tax of approximately £267 million

3.8 Data Analysis

Data analysis was accomplished by used excel sheets, SPSS, Strata and regression methods. This was possible given the nature of this research and for this reason; statistical data was emphasized on to enhance quantitative aspect of the research. The information in the next section will be presented in the graphical and table format and in order to merge the results with the main study questions, a brief explanation, analysis and discussion accompanied each table and graphs.

3.9 Ethical Consideration

As far as ethical consideration is concerned, the following guidelines were taking into account during the research period. Firstly, dignity and wellbeing of respondents who were used in collecting primary data was protected during the study. Secondly, the data obtained were treated confidentially during the study period.

3.10 Reliability and Validity of the Research

The reliability concept refers to the ability of the study to show a consistent result. A research study may combine a number of data collection methods such as qualitative and quantitative. For this case, the combination of secondary and primary data helps in increasing the study reliability. Given that qualitative data derived from secondary sources lack explicitly, primary data collection through questionnaire survey provided synergies thus improving internal reliability of the study. The use of internal reliability and re-grounding approaches helped to protect data integrity. On the other hand, external reliability was enhanced since questionnaire is a stable instrument that is quantifiable.

Validity of the research is concerned with the ability of the study to investigate major claims of the research. In the first place, it is my assumption that the samples that were used in the primary data collection are representative however; assigning subject randomly to the respondents posed a great challenge. In order to guard internal validity, an extensive literature review was done which covered main areas of investigations. A relatively large sample size helped in improving reliability and validity of the study.

3.11 Limitation of Research

There are some limitations associated with the study most of which are associated with accuracy and data collection. The use of secondary data presents problems because it affects the overall reliability and validity of the research. Primary data collection also compromised the results since it wholly dependent on the informants' knowledge on the question and this affected data accuracy. Though internet has simplified data collection and findings, its accuracy is highly questionable. On the other hand, the regression model applicable was somehow cumbersome because it required the use of data analysis tools such as SPSS, Excel and other applicable software. In this case, accuracy of the data sources must be analyzed to improve accuracy, reliability and validity. Another limiting factor was noted between information availability and time. As the research still continues under this topic, there is risk of excluding important information on the topic.

3.12 Conclusion

The methodology used in this study was geared towards gathering adequate information that would address the main requirements of the dissertation. That's why, primary data was subjected to regression analysis whereas secondary data was comprehensively covered at the literature review section. In the questionnaire, the number of respondents was adequate to help in the interpretation of the situation at hand. On the other hand, research designs, philosophy, approaches, methods and philosophy were also explained in this chapter. Other areas covered in the chapter include methods of questionnaire administration, limitations of the study, reliability and finally, the validity of the collected data. After the presentation of the research methodology, the next chapters will be empirical in nature.