Letter from a worker in the UK sub-prime mortgages sector

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As house prices fall at their fastest pace since 1995 and the Financial Services Authority warn of "very difficult" economic conditions to come, we publish the following letter from a worker in the UK sub-prime mortgages sector.

I have been working in the sub-prime mortgage sector in the UK for a number of years now. Here are some of my experiences of what is happening and where I see things going.

While the media has concentrated on the financial credit squeeze precipitated by the sub-prime market crisis, there has been little made of the huge social consequences of this crisis for the workers employed in the industry.

So far it has been the smaller sub-prime lenders, packagers and brokers that have laid off staff, but that will change when the big lenders finish their redundancy consultations. Victoria Mortgages, which is in a similar situation to Northern Rock and went bankrupt in August, but was not bailed out with tax payers' money, has gone into liquidation with around 60 job losses.

Perhaps the largest redundancies will come from SPML, which is owned by Lehman Brothers and is in the process of shedding upwards of 225 people, nearly one-third of its workforce. GMAC RFC has recently announced it is to close High Street Homeloans, its sub-prime division with around 200 people going. Advantage Home Loans, part of the Morgan Stanley group, has announced 90 redundancies and MD Nationwide, a small brokerage company, is cutting 17 jobs. Mortgages PLC, owned by Merrill Lynch, is to shed 20 percent of its 325-strong workforce. Another MerrillLynch company, Wave**,** which deals mainly with prime business (that is people with good credit records), is shedding 20-25 staff. Finance brokers *blackandwhite.co.uk* is to make 50 job cuts. Kensington Mortgages, which is owned by Investec, will shed 65 jobs.

Recruitment consultants have warned that as many as 30 percent of workers in the industry could lose their jobs. Some analysts have debated whether Merrill Lynch will keep its sub-prime business at all and many companies mentioned above will not survive into 2008 in their current form. Lehman Brothers for instance has already scrapped its second charge company LMC (London Mortgage Company), dealing with people who already have a mortgage but would like to raise extra capital secured against their home.

According to information from Moneyfacts, home loans have been cut by 41 percent and 6,400 mortgage products have been withdrawn, the majority in the sub-prime side of the business.

At the moment I work for a small broker. To say that the sub-prime industry is in a grave crisis would be an understatement. This is certainly the worst financial crisis in close to two decades. In the last three weeks I have witnessed at first hand lenders taking whole product ranges away and a growing number of lenders and intermediaries pulling out altogether. Many more will follow suit.

As you can see from the job cuts above it is the workers, many of whom are very low paid, who have borne the brunt of this crisis. While many people have made fortunes, including my own boss, out of sub-prime lending it will be ordinary workers and borrowers who will pay the price.

In my present job I would say that over 90 percent of mortgages that we broker are two- or three-year fixed rate and interest-only mortgages—that is, mortgages that carry a fixed rate for the first two or three years but then revert back to a rate that is usually three or four times above the previous fixed rate. Also in the short time I have been with this broker I have seen nearly all the mortgages being offered at interest only, that is, the person getting the mortgage is only paying off the interest of the loan over, say, a 25-year period with the capital still remaining to be paid off at the end.

According to the Council of Mortgage Lenders about

1.3 million borrowers took out fixed-rate mortgages in 2005 and a further 1.5 million in 2006. Most of them have had their mortgages fixed for two years, but now face increases of between 0.75 percent and 1.5 percent on their mortgage rates. For the average mortgage of £114,000 this means a rise in repayments of about £102 and for those on an interest-only basis, £143.

To comply with regulations by the Financial Service Authority interest-only customers are supposed to have some sort of repayment vehicle in place such as a savings account to pay off the capital when the mortgage period ends. However, in the majority of cases this is wishful thinking. What you are going to have is people losing their houses and repossessions reaching previously unheard of numbers.

Hundreds of thousands of people are coming to the end of cheap fixed-rate deals, but many lenders do not know how many of those who have taken out interest-only loans with them are able to repay the capital.

According the Capital Economics, an independent macroeconomic research consultancy, over 360,000 homebuyers over the past two years have taken out sub-prime or self-certificated loans for which they do not have to prove their income. While in the past these types of loans would make up no more than 5 percent of mortgages, now they are around 30 percent. The most dangerous aspect of these types of loans is the level of fraud involved.

It is not for no reason that these loans are called "liar loans" in the United States. Many times I have seen brokers not only change the amount a person earns to fit the loan amount, but in large numbers of cases they actually change a person's occupation. If someone does not earn enough to qualify for a mortgage, they will suddenly *become* self-employed with an inflated salary. Or they will suddenly have large amounts of overtime and bonuses which, in some cases, amount to more than their basic salary. These figures are self-certified in many cases and a lender will turn a blind eye to them as most of the sub-prime lenders do not carry out a check.

Another aspect is what is termed "creative accountancy." On numerous occasions I have seen bank statements no longer showing a debit. In extreme cases documents are forged, with companies that do not exist suddenly appearing on paper. There is even a web site that specialises in providing fake utility bills, payslips, etc., which while not illegal, is reported to receive a large amount of its custom from the mortgage industry.

An important change over the last five years or so is that people who would normally be mainstream borrowers have been pushed into the risky sub-prime market. In 2006 about a fifth of all loans could be classed as high risk, i.e., more than 4.5 times someone's income or more than 100 percent of the property price.

It is clear that many borrowers are already struggling. A staggering report from the housing charity Shelter claimed that a million people are using their credit card to pay their mortgage or rent. Between January and March 2006, over 30,000 people went bankrupt or took out an Individual Voluntary Arrangement (IVA)—more than 330 personal insolvencies for every day of winter. It has been reported that 2007 will be the worst ever year for personal insolvencies in England and Wales, surpassing last year's record total of 107,288.

As more and more people are finding that even a loan in the sub-prime industry is out of their reach they are forced to turn to even more predatory lenders. These include the long-standing "alternative credit industry," the licensed door-step credit companies, also known as weekly collected credit or home credit, and pawnbrokers and moneylenders who operate virtually out of sight. There is also a host of new and virtually unregulated entrants onto the high street that employ a range of sophisticated and hard-sell tactics.

According to Datamonitor, the market research agency, the door-step market is worth more than £3.3 billion a year, with customers borrowing an average of £1,000 a year. A typical APR on a loan of £60 repayable over six weeks is 500 percent, but much higher rates are not unusual.

The worst problems arise when borrowers run into difficulties with repayments and are offered rollover loans to cover debts built up on their first loan. Britain has seen the debt collection industry quadruple in size since 2003 as people have gone into the red in record numbers. The industry now handles £22.7 billion now as opposed to £8.6 billion in 2003. The figure is set to rise to £24 billion, but given the current financial situation even this is a conservative estimate.