

It is often said that, if we want to understand the present and, more importantly, look into the future, we need to start with history. This maxim is usually brought into play when discussing such weighty matters as the power struggles between great nations, or how we are ruled and governed – but it also holds true when looking at the market dynamics of our own sector. In particular, if we want to speculate on how the packaging sector will develop in the future, we need to understand how it got to where it is now.

Tipping point

Looking back to the late 1980s, most informed commentators would probably agree that the tipping point for mortgage packaging was provided by Stephen Knight's Private Label. Market conditions included, on the one hand, cash-rich lenders keen to lend and, on the other hand, insurance company mortgage desks with huge distribution potential created by their large field sales forces. Private Label stepped into an entrepreneurial role between the lenders and the brokers by offering to take basic applications, package them, and present them to lenders, ready for offer. At the same time, by offering lenders this easy route to bulk distribution, Private Label was able to work with them on designing products that the insurers' mortgage desks could sell with ease. As these products started to cater more and more for the needs of niche and non-conforming customers, this boosted the mortgage intermediary sector by supplying it with products that could not be accessed by consumers directly from lenders.

Clearly, the role played by this sort

of mortgage 'wholesaler' added value to both ends of the chain. Intermediaries could sell more mortgages without the administrative burden of packaging the applications, and lenders could enjoy far wider distribution and reduced administrative costs. Therefore lenders wishing to use the intermediary route to boost sales were happy to pay the middleman for its services as well as paying the intermediary's procuration fee. Sounds familiar? We may not have called it 'packaging' in those early days, but the core concept had been established.

Meltdown

The next set of historical circumstances that helped to boost the significance of the packaging function came together in the early 1990s, when economic downturn and high interest rates prompted a housing market crash and personal debt problems going into meltdown. Although it may be hard to believe in the enlightened 21st century, in 1993 there were 1.8 million CCJs issued; 58,500 properties taken into possession – down from a peak of 75,500 in 1991); and, at the end of 1992, 826,000 mortgage accounts with arrears of three months and more. These millions of people with newly acquired adverse elements in their credit records still needed somewhere to live, and a mortgage loan with which to purchase that property. Unfortunately for them, the credit scoring systems being implemented by high-street lenders took a dim view of CCJs and arrears, and would simply decline their applications.

Such a vacuum in the marketplace could not last for long and, by the middle of the decade, the new breed

of non-conforming lenders started to establish itself, spearheaded by Kensington. Operating according to credit policies that priced products to cover the added risk realistically, these lenders raised funds in the wholesale money markets and by successfully securitising their loan books. They were lean and hungry lending machines with lots of cash to pay third parties to originate business for them and package the applications.

Dealing with non-conforming applications was, and still is, not as straightforward as introducing prime credit mortgage cases, and took a lot more time and effort. Acknowledging this extra workload, lenders paid generous packaging fees which, in turn, encouraged large numbers of new packaging firms to enter the market.

Influencing strategies

By the beginning of the third millennium, major changes in mortgage processing had started to influence lenders' distribution strategies. The power of web-based communications and data transfer was being realised, and each advance that was made in this direction seemed to reduce the need for the sort of paper-based information that mortgage packagers had hitherto sourced. At the same time, competition in the lender market was starting to drive down product pricing and squeeze profit margins. Unsurprisingly, lenders' thoughts started turning to the direct-from-broker origination route, which would enable them to reduce costs considerably by cutting down on their packager fees.

The most recent historical event that also appeared to threaten the existence of the packager community was the build-up to and implementa-

A packaging history



Vic Jannels charts the history of the mortgage packager and considers what the future holds for the sector

tion of Financial Services Authority (FSA) regulation in November 2004. The packaging function, and its role with regard to giving advice to would-be borrowers, did not fit easily within the FSA's definitions of what constituted the mortgage advice and sales process. So, when the time came to apply for authorisation, some packagers were faced with a 'Catch 22' situation. Many lenders, determined to be as squeaky clean as they possibly could be with regard to the FSA's requirements, were putting out the message that they would only deal with authorised firms. On the other hand, packagers that only dealt with brokers and did not have a direct-to-consumer operation could not be FSA-authorised because they did not carry out any regulated activities. For a time this appeared to pose a real threat to the continued existence of 'pure' packager firms, but in reality the majority of packagers were able to become regulated and those who did not, have been able to trade successfully alongside the other regulated parties.

The future

So much for the historical build up – but where does packaging stand now and what does the future hold? One thing is obvious – lenders cannot afford to ignore the bulk distribution power both of larger individual packagers and packager associations. Packager associations are now a well-established part of the mortgage distribution marketplace and no doubt we will see more of them emerge to serve the unique needs of their member firms. One thing they all have in common is the ability to deliver results to lenders in the form of guaranteed distribution and supply brokers with keenly priced exclusive products and top quality service standards.

Will the packaging sector survive in the long term and can it continue to offer valuable service to lenders and brokers in order to do so? I believe that the answer to this lies in the historical roots of packaging – i.e. lenders needing a steady supply of good quality cases on which to write

profitable business and individual brokers needing a shoulder to lean on when they are faced with a non-standard customer.

Taking lenders first, it is an indisputable fact that packaged applications have a far higher success rate than applications direct from brokers. In 2001, the PMPA did its own research among its lender panel that revealed less than 50 per cent of broker-introduced applications reached offer stage as opposed to 85 per cent of packager-introduced business. On the broker side, too, packagers can offer a very attractive combination of benefits. Brokers cannot possibly have the overall experience and up-to-the-minute knowledge of lender criteria and processing times that will exist within larger packager firms.

A lot has happened to the packaging sector over the last 15 years, and we are still evolving. Overall, the evidence all points to a thriving packager sector, delivering added value to lenders and brokers, for the foreseeable future.

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