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Mortgage refinancing – from whom to whom?

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Abstract

A diverse set of entity types operate in the Irish mortgage market. We explore the role of these various bank and non-bank entities in mortgage refinancing patterns from 2017, looking at both *from whom* mortgage borrowers switch, and *to whom* they switch, using rich credit registry data. Looking at where borrowers *switch to*, we show that non-bank lenders are a particularly cyclical, interest-rate-sensitive source of financing, consistently increasing their share of mortgage switchers from 2019 to the turning point of the interest rate cycle in mid-2022, followed by a collapse in switching market share in late 2022 and 2023. On the question of *from whom* mortgage switchers originate, we highlight that mortgage customers at non-lending non-bank firms had a structurally lower propensity to switch than customers of banks over the period 2017 to 2023. However, higher-credit quality portfolios at these servicers have had similar rates of switching to those at retail banks, while those with higher credit risk are the groups that have had lowest propensity to switch.

1 Introduction

Mortgage refinancing, or switching, is a key determining factor in domestic financial stability and in the strength of transmission of monetary policy to household finances and the wider economy. Switching, and in particular fixing a mortgage interest rate, can lower up-front borrowing costs and insulate a borrower from future increases in interest rates, improving the resilience of the household sector to shocks. These decisions have implications for cash flow and consumption across households, and can have broader implications for the economy. The Central Bank has identified mortgage switching as a priority topic for consumers, as previous research has concluded that historically, many borrowers did not avail of the potential savings on offer from mortgage switching (Byrne, Devine and McCarthy, 2020).

In this *Note*, we complement the recent work of Scott and Singh (2024) by building a "from whom to whom" matrix of mortgage switching, with a focus on the types of mortgage providers involved on both sides of a mortgage switch between 2017 and late 2023. Our data source, the Central Credit Register (CCR) enables a detailed assessment of the role played by retail banks, credit unions and non-bank lenders as the *destination* for mortgage switchers, shedding light on the competitive role of these lender types across distinct interest rate regimes. Additionally, the data allow us to track the *previous lender* prior to mortgage switching, to compare how readily customers of banks and non-bank non-lenders (or mortgage servicers) have been able to switch mortgage provider. This level of detail on lender types offers a globally unique insight into the functioning of the mortgage

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market. Our work also updates Scott and Singh (2024) by including the period of higher interest rates in 2022-23.

2 A recent history of mortgage refinancing

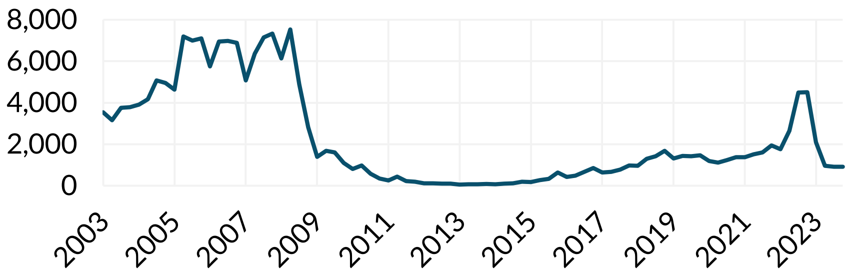
Published data on mortgage switching are available since 2003, and are shown in Figure 1. Mortgage switching was at a historical peak of between 6,000 and 8,000 loans per quarter between 2006 and 2008, a period of intense mortgage market competition. In late 2022, switching rates increased sharply to levels last seen in 2004, while remaining below the historical peak.

The BPFI data used in Figure 1, as well as the CCR data used in subsequent sections, cover switching *across mortgage providers*. It is important to highlight that borrowers can also avail of mortgage savings by changing mortgage products *at the same lender*, without switching. This activity is not captured in either aggregate or micro data sets on switching discussed in this paper.

The trend is Figure 1 shows that mortgage switching behaviour is connected to the broader financial cycle, with a number of distinct periods identifiable:

- a peak in 2006-2008, when credit conditions were unsustainably loose and competition among lenders was intense;
- a deep trough in 2009-14, in the aftermath of the global financial crisis, as lenders' balance sheet capacity was eroded and the appetite for new lending was at historic lows;
- a gradual but small increase during the economic recovery period from 2015 up to 2022;
- a rapid and dramatic increase at the turning point in the monetary policy cycle in 2022;
- a fall as higher interest rates transmitted to the Irish mortgage market during 2023.

Figure 1: Number of re-mortgages, per quarter



Source: Banking and Payments Federation Ireland Mortgage Drawdowns.
Notes: Number of re-mortgage (switching) loans granted by BPFI member institutions between 2003 Q1 and 2023 Q2.

3 Data and results

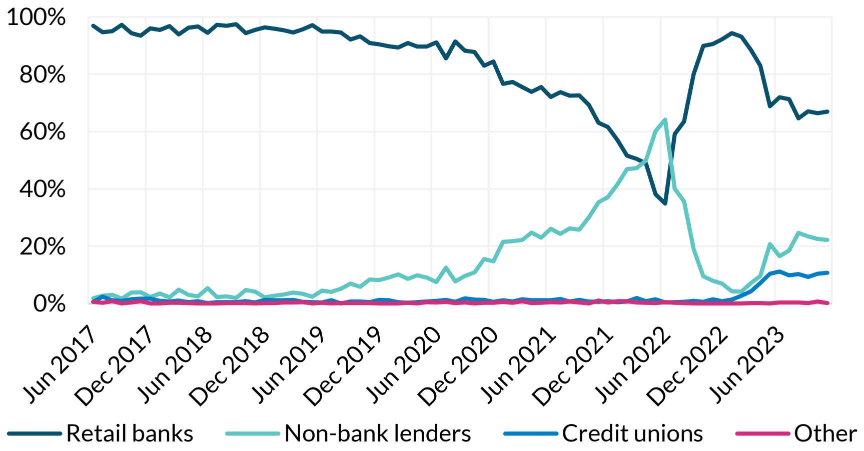
3.1 To whom?

Using the CCR, we first focus on the "*to whom*" side of the mortgage refinance. The CCR confirms that banks were the predominant destination for over 90 per cent of all mortgage switchers between 2017 and 2019 (Figure 2). The share of mortgage switchers who moved to non-bank lenders then increased from 20 per cent at end-2020 to 60 per cent in mid-2022, coincident with the loose financing conditions of the Covid-19 pandemic. This is consistent with findings on new mortgage lending from Gaffney et al. (2022).

In an accompanying paper, Scott and Singh (2024) highlight that non-bank lenders were "leaders" in the interest rate cycle in Ireland. By competing on mortgage interest rates, they transmitted loose monetary policy to borrowers in the Irish mortgage market. Our findings also build on previous work by showing the cyclicality of non-bank lending during the tightening phase: after the mid-2022 increases in ECB interest rates, non-bank lenders were the destination for less than 10 per cent of switches. Our findings are in line with international research which shows that non-banks lend more during periods of loose financial conditions and tighten credit more rapidly in periods of tight financial conditions, because they typically rely on volatile and cyclical forms of market funding due to a lack of insured deposits (Moloney et al., 2023).

Finally, the CCR data reveals that in recent months credit unions have begun to account for a small but growing share of mortgage switches. From a position of having been close to absent from the mortgage switching market up to late 2022, around 10 per cent of mortgage switches were to credit unions by the end of 2023.

Figure 2. To whom? Share of mortgage switching per month by destination, July 2017 to December 2023



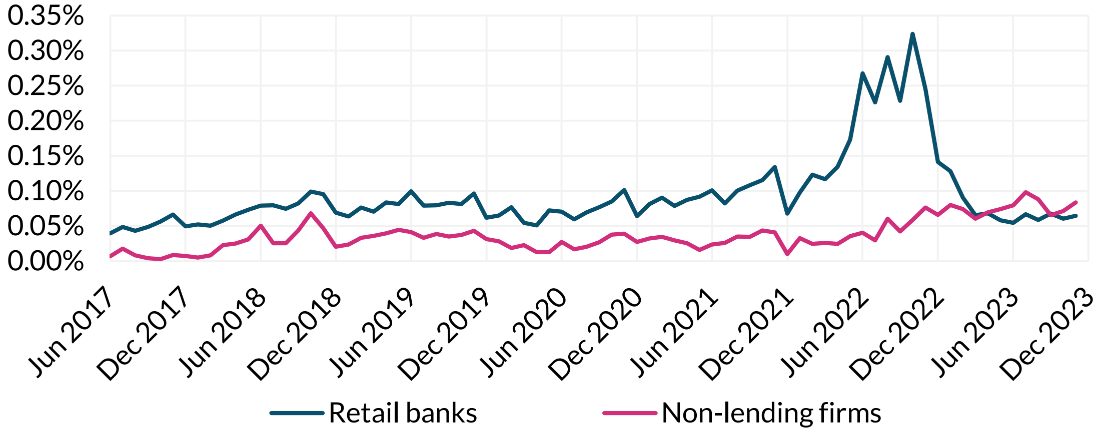
Source: Central Bank of Ireland Central Credit Register.
Notes: Monthly data showing shares of switcher mortgages, as identfied by Central Bank of Ireland internal calculations, based on the type of lender to which the switcher borrower moved.

3.2 From whom?

A key policy question in Ireland since mid-2022 has related to the varying degree of monetary policy pass-through across mortgage borrowers (Byrne et al., 2023). Along with tracker mortgage borrowers, whose mortgage rates are contractually bound to ECB interest rates, another particularly affected group were customers of “non-lending firms”: non-bank servicers that hold portfolios of mortgages but do not issue new mortgages. Some customers of these firms were experiencing interest rates close to 7 per cent by mid-2023 (Cassidy and Sarchi, 2023), and switching away to a lender offering lower rates would have allowed borrowers to improve their financial position.

The CCR allows a detailed comparison of switching behaviour among customers of retail banks and non-lending servicer firms, which together account for 95 per cent of Irish residential mortgages. Figure 3 shows switching rates per month from July 2017 to December 2023 as a share of all mortgages at these providers, regardless of the destination of the switcher.

Figure 3. From whom? Switching rates of mortgages per month, by previous provider, July 2017 to December 2023



Source: Central Bank of Ireland Central Credit Register.
Notes: Monthly data showing the shares of all mortgages that ended due to mortgage switching, as identfied by Central Bank of Ireland internal calculations, based on whether the lender prior to the switch was a retail bank or a non-lending firm.

The first key insight is that customers of banks were much more likely to switch than customers of non-lending servicer firms between 2017 and early 2023. In particular, the increase in mortgage switching during 2022 was driven by customers of banks. The most likely reason for the difference was the lower average credit quality of customers of non-lending firms, making it more difficult for the average borrower to meet the credit standards of a new mortgage lender. As an example, the share of PDH loans that were in mortgage arrears in 2023 was 3.4 per cent at retail banks, versus a much higher 23.8 per cent at non-banks.

Second, despite a gradual reduction in Irish mortgage interest rates from 2015 onwards, mortgage switching increased sharply only in 2022, around and shortly after the start of the period of increasing ECB interest rates. By the end of 2022, mortgage interest rates had increased sharply and contribution to a reduction in the propensity to switch among bank customers back to 2017 levels.

Finally, switching away from non-lending firms increased gradually in 2022 and 2023, despite the rise in mortgage interest rates across the market. Several reasons may explain this growth in switching by customers of non-lending firms. First, their high average interest rates meant that there were still potential gains from switching even as market interest rates rose. Second, there was heightened public scrutiny during that period on the capacity of non-lending firms' customers to switch to banks, including through Central Bank of Ireland supervisory activity.

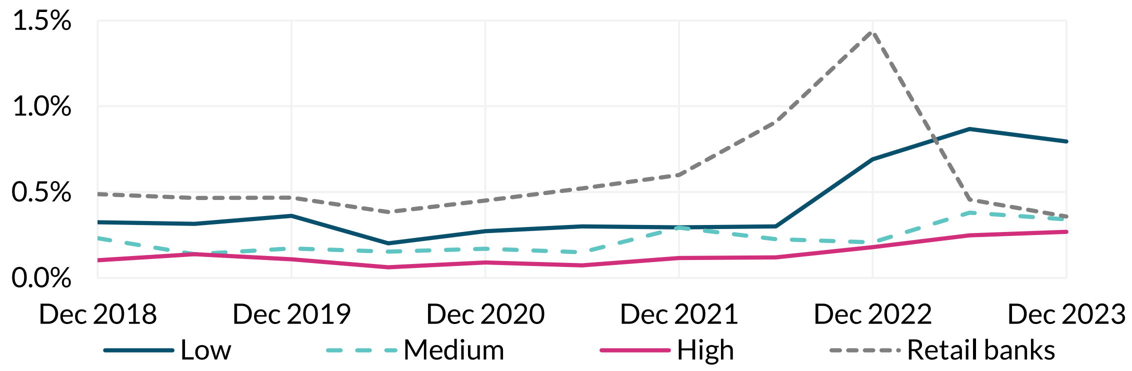
The Central Bank has investigated lower switching rates out of non-lending firm mortgage portfolios as a key question for consumer protection. Supervisory work in this area in 2023 concluded that there was no blanket impediment or barrier to switching in place. Our assessment of the CCR evidence supports these conclusions. Based on a combination of borrower characteristics and information on the historical origins of the portfolio, we classify non-lending firm mortgage portfolios into three groups: High, Medium and Low credit risk.[2] Our hypothesis is

[2] "High" credit risk portfolios were predominantly composed of Non-Performing Loans sold by retail banks, whereas "Medium" and "Low" risk portfolios contained a mix of sources and of borrower types, such as portfolios sold earlier in the 2010s by banks exiting the Irish consumer market.

that, if *blanket barriers* to switching were in place, then the switching rates of the High, Medium and Low risk portfolios would all be of a similar level.

Figure 4 illustrates that blanket barriers to switching do not appear to have been in place. High and Medium risk portfolios have had very low switching rates throughout the period. However, Low risk portfolios at non-lending firms saw their switching rate rise in mid-2022, as interest rates began to increase, and this continued throughout 2023. In recent months, the switching rate away from non-lending servicers with a Low risk profile was higher than that for customers of retail banks.

Figure 4: Mortgage switching rates among non-lending firm customers per half year, by risk group, 2018H2 to 2023H2



Source: Central Bank of Ireland Central Credit Register.
Notes: Half-yearly data from 2018 H2 to 2023 H2. Mortgages are categorised based on the overall risk characteristics of the portfolio sold by the original lender. Grey dotted line shows switching rates among customers of retail banks, for comparison.

4 Conclusion

Our work highlights the usefulness of high-quality granular data for policy insights. We use the Central Credit Register to offer new insights on the timing of switching behaviour through the monetary policy cycle, the sharp increase in switching activity at the turning point of the cycle, and the key role of non-bank lenders in switching activity. Finally, the data allow new insights on the extent to which borrowers at non-lending servicer firms have been able to switch their mortgage, showing that while over many years borrowers at these servicers had much lower switching rates, this has gradually increased since 2022 and has been higher than the switching rate away from retail bank mortgages in recent months.

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