

CCPC ADVICE HELPS CONSUMERS JUDGE MORTGAGE OFFERS, BUT POTENTIALLY SERIOUS MISUNDERSTANDINGS REMAIN

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LUNN



CCPC advice helps consumers judge mortgage offers, but potentially serious misunderstandings remain ¹

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INTRODUCTION

Although many mortgage-holders stand to make substantial savings by refinancing or “switching” their mortgage, very few do so. In collaboration with the Competition and Consumer Protection Commission (CCPC), the ESRI’s Behavioural Research Unit undertook a controlled behavioural experiment with a sample of mortgage-holders. The experiment was designed to test whether reading independent advice on how to evaluate mortgages and navigate the switching process can help consumers to make better choices. The study also assessed how well mortgage-holders understand the basic features of mortgages.

METHOD

A representative sample of 110 people with a mortgage took part in a controlled laboratory experiment. They evaluated 24 mortgage offers and rated how willing they would be to switch to each of them. Important features, such as the APR and cashback amount, were different for each offer. Halfway through the experiment, the participants read advice from the CCPC’s ‘Switching Your Mortgage’ webpage. By comparing answers before and after reading the advice, the experiment tested how reading the advice altered participants’ judgements. Thus, the experiment was a controlled test of which features were most attractive before and after reading the advice. The study also tested how the advice affected mortgage-holders’ perceptions of the switching process and their confidence when judging

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This Bulletin summarises the findings from: Timmons, S., Barjaková, M., McElvaney, T. J., & Lunn, P. D. (2019). Official Advice Improves Mortgage-Holders’ Perceptions of Switching: Experimental Evidence, *Behavioral Public Policy*, 1-29, available online: <https://doi.org/10.1017/bpp.2019.38>

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offers. Lastly, the experiment used multiple choice questions to measure how well the mortgage-holders understood mortgages.

RESULTS

Before reading the advice, while mortgage-holders were somewhat more willing to switch to a lower APR, they were strongly enticed by high cashback offers. On average, participants were willing to take an APR increase of 0.39 percentage points over the lifetime of the mortgage in exchange for €2,200 in additional cashback. For the average mortgage, this exchange amounts to taking out a loan of €2,200 at an interest rate of 24.2%. However, after reading the advice, mortgage-holders' judgements changed. They were much more attracted to APR savings and less enticed by cashback offers. They also become more sensitive to the remaining term of the mortgage, i.e. years left to pay off the loan. In other words, after reading the advice, participants gave more weight to factors that result in long-term savings.

The results also showed that those who initially knew less about the switching process became more likely to switch after reading the advice than before. Consumers in general felt more confident judging mortgage offers after reading the advice.

Nevertheless, answers also revealed potentially serious misunderstandings. When asked what would be required in order to switch, just one third of consumers listed the requirement to engage a solicitor and only one quarter listed the need to have their property revalued. Yet these two factors typically constitute the largest transaction costs in switching. Moreover, three-in-four mortgage-holders misunderstood the consequences of repaying only the interest on a mortgage and one-in-ten misunderstood their debt liability were they to fall into arrears.

CONCLUSION AND IMPLICATIONS

Broadly speaking, the findings imply that reading CCPC's online advice makes a difference. Before reading it, consumers were rather insensitive to APR gains and were instead drawn to mortgages with high cashback offers. After reading the advice, they were less tempted by cashback and more sensitive to APR and the length of the repayment term. In general, therefore, the official advice led mortgage-holders to place greater weight on factors that deliver long-term savings. Recent regulatory changes require lenders to direct consumers to the official advice and the current findings lend support to this approach.

However, the results also imply ongoing serious issues with consumers' perceptions of mortgages. Participants in the experiment had previously purchased a mortgage. Yet, before reading advice, they were arguably disproportionately influenced by cashback offers, which are pervasive in the Irish mortgage market. Furthermore, a significant proportion were unaware of key steps needed to refinance and a large minority held serious misunderstandings about repaying their mortgage and their own debt liability.

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