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The UK property market is starting to feel the impact of the steady rise in interest rates. Recent figures from the Council of Mortgage Lenders (CML) indicate that the number of mortgage approvals for house purchases is running 15 per cent below the high levels of Autumn 2006, and is at the lowest level since April last year. However, while this suggests that potential buyers are being put off at the current time, the CML views this as temporary and that activity will restart as soon as rates have peaked.

First-time buyers are certainly feeling the squeeze of higher interest rates. According to a recent survey by mform.co.uk, over two million have admitted to struggling with their mortgage repayments after the recent Base Rate rises. Another quarter point increase would inflate the number of those struggling even further, and perhaps push many over the edge into arrears – particularly those just coming out of a two-year fixed deal who could see their mortgage rates adjust by as much as two per cent.

Fixed rate products can protect consumers against rising rates during their term, but they provide no protection against changes in personal circumstances. First-time buyers, acknowledged as being more vulnerable than any other category of home owners, are the least likely to have sufficient savings to cope with facing a significant hike in repayments or the loss of employment, illness or injury. Yet at a time when arguably mortgage payment protection insurance (MPPI) could provide a much-needed safety net, take-up is falling and currently less than 20% of all mortgage holders are supported by MPPI according to CML statistics. The Competition Commission's investigation into payment protection insurance (PPI) including MPPI has spurred on a vast amount of negative media coverage about these products, and the resulting effect is that take-up is falling.

So how is the PPI industry responding to all the negative comment and what is it doing to encourage consumers that the product – particularly MPPI – can provide a reliable safety net when needed?

With the media pointing its finger accusingly, the Competition Commission inquiry and the ongoing thematic review by the Financial Services Authority (FSA), it is not surprising that those in the PPI market are feeling battered and bruised by the criticism. While the investigations are taking place it would seem that rather than embracing the opportunity to improve their products and sales processes, the majority of

PPI providers and distributors have been frozen into a state of paralysis. So what are the implications of inaction for the industry and consumers?

To be frank, apart from a few tweaks, the PPI proposition has not evolved a great deal since it was pioneered in the UK in the 1970s. However, during this time, we have seen significant changes in society that should have driven advances in PPI. We have seen a shift in cultural attitudes towards spending and a willingness to take out and increase borrowing as well as go into the red. According to the national money education charity, Credit Action, almost 20% of Britons have got into debt by spending on credit in anticipation of receiving a pay rise or work-related bonus, and six per cent admit to going into the red most or every time they go on holiday. At the same time, the distribution model itself has undergone a sea change allowing consumers to spend and borrow at the touch of a button via telephone, ATM banking and the Internet. Although there have been a few instances of innovation within the PPI market over the past couple of years such as the introduction of age-banding, one could argue that its products have, on the whole, remained static. The homogenous product introduced in the 1970s is primarily the same product that the majority of policyholders buy today.

Up until now, market dynamics have played the most influential role in preventing the PPI industry from keeping up with the times. PPI has historically been sold almost exclusively through third party distributors. Their enormous bargaining power combined with increasingly sophisticated procurement practices have resulted in a greater focus on margins, rather than on product innovation and driving value through to the consumer.

It could also be argued that the relationship between PPI sales and APR rates has also played a role in stemming innovation. The sale of PPI and the sale of the credit product have been inextricably linked over recent years and created a tremendously successful business model for many distributors of the product. The income stream generated has been so great in relation to the level of investment required that the old argument of “why fix it if it ain’t broke?” seems to have been the philosophy employed to date.

Add to this the requirement to keep the sales process simple, even though it may conflict with the needs of the consumer, plus an apathetic culture resulting from a self-regulating industry and it is not hard to understand why PPI products today are not that dissimilar to the products offered almost 40 years ago.

Currently, however, the greatest factor influencing how the PPI industry develops is the various market investigations. In November 2005, before there was talk of the Competition Commission’s investigation, Mintel forecast that the PPI market would reach £8,154 million by 2009. In January 2007, it revised its forecast to just £4,964 million in 2009. Many industry players appear to have been frozen into inaction as they await the outcome of the current Competition Commission inquiry, which is expected at the end of

2008. Equally, hefty public fines from the FSA for mis-selling have even led a few companies to pull out of PPI altogether for fear of reputational damage.

The question that begs to be asked is how many distributors or third parties are brave enough to enter the PPI market now given the current state of play? With existing PPI distributors displaying a huge degree of caution in their lack of appetite to move their books of business and insurers appearing reluctant to invest and develop their product offerings, the PPI market is in a state of paralysis. This is bad news for the industry as it can only exacerbate the market's already faltering reputation.

In my view, it is more important than ever that the PPI industry invests in new product development and pricing regimes and encourages new distributors to enter the market. This is the only way we can build and sustain the proper level of competition that the Competition Commission is surely looking to achieve and, ultimately, deliver greater choice and better deals for consumers.

When we consider the consumer's point of view, it is hardly surprising that they are skeptical of the value of PPI given all the negative media coverage. The Sunday Times described PPI as "the biggest scandal since endowments" and the Daily Mail described the Competition Commission investigation as a "probe into £1bn loan insurance blackmail." But consumer debt is at an all-time high of £1,325 trillion (Bank of England, April 2007). Without protection, many are at serious financial risk should their personal circumstances change. Moreover, first time buyers are now able to take up mortgages that are more than five times their salary with an LTV of 90 to 100 per cent, interest rates are likely continue to rise and house prices will remain high. Yet an alarming one in four of the total UK population have no savings at all and a further 25 per cent have less than £3,000 to fall back on. Half the population could survive financially for just 17 days should they suffer an unexpected loss of income, according to research by Combined Insurance. No one wants to see a repeat of the 1990s housing market crash. For the last 15 years we've been fortunate that the economy has been buoyant and the safety net that MPPI provides has not been tested. However, we are experiencing an increase in possessions. The question begs to be asked as to how many of these could have been avoided had more mortgage holders taken out an MPPI policy.

It is a recognised fact that payment protection insurance has real value. It acts as an important risk management tool for consumers and lenders alike. Clive Briault, FSA managing director of retail markets, said: "When sold properly, PPI can provide worthwhile protection against changes in personal circumstances."

It is up to the industry to take positive action to improve the products and sales process so that the true value of PPI can be redeemed. This could mean reducing all income to a level where distributors are happy to disclose it. It definitely does mean that we should not treat all customers as a homogenous group. We need to design, manufacture and distribute products that are flexible enough to meet the needs of individuals and make them accessible and affordable for all. Ultimately, providers and distributors need to work together to close the gap between consumers' needs and market practices today.   To bring these advances to fruition will undoubtedly require financial investment, particularly as many insurers are still burdened with legacy systems that will not be able to cope with the demands that new products and pricing structures will place on them.

It is going to require a fundamental shift in mindset at board level to ensure that PPI is deemed a priority now if an organisation is serious about maintaining its market position, and not something that is 'on standby' until the investigations are over. After all, what is the alternative? To play it 'safe', remaining in a state of paralysis until the outcome of the Competition Commission? I believe organisations taking this strategy are suffering from a false sense of security. Those that will prosper, despite the investigations and negative press, will be the ones that anticipate the changes and start introducing the much-needed innovation today.

Competition Commission key milestones

2007	
7 February	Reference made by Office of Fair Trading
February – March	Request for off-the-shelf material; advertisements; letters to third parties; etc
April	Statement of issues published and questionnaires issued
March - June	CC visits and hearings with main and third parties
September/October	"Emerging thinking" notified
November/December	CC further hearings with parties
2008	
January	Deadline for all parties' responses/submissions required before provisional findings
February/March	Notifying provisional findings and (if required) possible remedies
April/May	Report if no adverse effect on competition; or remedies hearings (if required)
April	Final deadline for all parties' responses/submissions
June	Provisional Decision on remedies (if required)
August/September	CC publishes report
2009	
6 February	CC statutory deadline (may be completed in a shorter time)

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