

Interest rate pressures, rising mortgage stress and a tighter credit market present a challenging backdrop to a new parliamentary inquiry into competition in the banking and non-banking sectors.

# Crunch time

STORY: GEOFFREY MASLEN

One newspaper headline told the grim story: “More pain ahead on homes front”. Another heading put a figure to the pain: “900,000 Australian households face mortgage stress.”

Mid-year estimates indicate the number could soon pass the one million mark given that each month another 35,000 families were joining the ranks of those struggling to meet their mortgage repayments.

As higher interest rates pushed more families over the edge, home buyers and other borrowers defaulted on payments by a record \$3.5 billion in the March quarter, according to the Reserve Bank.

In the 12 months to June, the Victorian Supreme Court issued more than 2,500 repossession orders against families that had failed to meet their mortgage payments. The annual figure for repossessions has tripled in six years.

Martin North, who heads Fujitsu Consulting, said mortgage stress is no longer confined to low-income suburbs but is affecting many households in affluent areas.

“This time around we have what we call ‘affluent stress’,” he said. “So people for example in Bondi and Chatswood, who traditionally have not had major issues, [do now] because of the fall in the stock market and the margin calls that have been created off the back of that. They suddenly find themselves in that higher stress category as well.”

The increasing cost of a mortgage, or even obtaining a loan to buy a house, is affecting the number of people who borrow from banks and other home lenders. The Australian Finance Group, which accounts for 10 per cent of the national mortgage market with a total book exceeding \$50 billion, declared in July that Australia was in a “mortgage recession” after two successive quarters of falling sales.

A spokesman for the group said average mortgages were still increasing because borrowers needed to take out bigger loans to cover the cost of housing. Whereas the average loan across Australia a year ago was \$317,000, it was now \$341,000, although the average in NSW was \$404,000. These big increases were squeezing people out of the market as they could no longer afford to take out even medium-sized loans.

The Reserve Bank raised interest rates 12 times between early 2002 and August 2008, adding three percentage points to mortgages, on top of the rate rises imposed by Australia’s banks as a result of the ongoing global credit crunch. It was these cumulative and collective rises, plus the unexpected and devastating impact of the higher cost of oil, that sharply added to the financial burdens Australian families now have to carry.

Banks are the biggest lenders to families wanting their own home and the biggest cause of their misery as the burdens increase. Now they have been accused of forcing their staff to persuade customers who cannot afford mortgages to take them out.

A survey by the Financial Services Union of its members working in the banks found that six in every 10 felt pressured to push what they regarded as inappropriate loans and other financial products. Staff who objected to excessive debt-pushing had been warned their jobs were at stake, the union said.

Growing public concern about rising interest rates and bank charges led federal Treasurer Wayne Swan to ask the House of Representatives Economics Committee to inquire into and report on competition in the banking and non-banking sectors.

As part of its terms of reference, the committee has been asked to examine competition in the retail banking and non-banking sectors, to pay particular attention to home mortgage products and linked facilities frequently offered to consumers, such as credit cards and savings accounts, and to “undertake a stock-take of the Australian retail banking and non-banking industries”.

House Economics Committee chair, Craig Thomson (Member for Dobell, NSW) said: “We need to open up competition in the retail banking and non-banking sectors, demystify the number of home mortgage products available and offer a wider choice to the consumer.”

That could not come too soon for many consumers. A writer called “Sydney”, in a comment published in the Suncoast Daily Online, referred to the newspaper’s headline: “Interest Rates Rise Again”. Sydney declared: “Wow! I have been in Australia for about 10 years now and can’t believe how expensive this country has become ever since. In all honesty I am planning to leave for that reason because there is not enough money to be earned to cover all those costs just to have a roof over the head and a normal, happy healthy life. It seems to be all we do is work for government and the banks in order to fill their never-ending pockets.”

He could be right: earnings from domestic fees charged by the 54 banks grew to \$10.5 billion last year, with income from household loans growing faster than that from businesses. While fees from business rose by 7 per cent to \$6.1 billion, bank earnings from households jumped by 9 per cent to \$4.4 billion.

The Reserve Bank says this partly reflects the wider take-up of housing loan packages, which have a sizeable annual fee but give households a lower interest rate on their home loans, and other benefits such as fee-free deposit and credit card accounts.

While the banks this year have faced the biggest surge in bad debts since records began in 1994, figures published on the Reserve Bank’s website show they still have total assets of almost \$1,900 billion—that is, \$1.9 trillion! The 14 building societies that provide housing loans have \$21 billion in assets, the 143 credit unions \$39 billion and another 117 finance companies have assets of \$116 billion.

Adding to mortgage stress, earlier this year banks moved independently of the Reserve Bank and raised interest rates. Early in July, St George Bank—the nation’s fifth-biggest lender—hit its 200,000 customers with a 20 basis-point increase in its standard variable home-loan rate. Almost immediately, the Big Four began to follow.

The increase by St George, together with rises in a range of deposit rates, lifted its variable home-loan rate to 9.67 per cent, well ahead of the other banks. But a week later, the NAB and Suncorp joined in the latest round of unilateral rises: the NAB

lifted its variable mortgage rate 15 basis points to 9.61 per cent while Suncorp equalled St George’s 9.67 per cent with a 20 basis-point jump. The other banks soon followed.

The consumer group Choice earlier this year said even small rate increases in the current financial environment could represent “the straw that broke the camel’s back”. Choice noted that borrowers increasingly had been feeling the pinch from a spate of creeping interest rate rises.

In Perth, Channel 7 interviewed Mary-Jane Fonti, described by the reporter as “the human face of middle Australia”. A mother of four in an average suburban mortgage belt, hanging on by the skin of her teeth like tens of thousands of Australian home-owners, Mrs Fonti said life was a day to day struggle.

“Rising interest rates, petrol hikes and falling property values have combined to see huge numbers of people facing repossession. If my children don’t get full-time work and are not able to help me then yes, we will probably have to sell the house,” she said.

City dwellers are not alone, of course. Mortgage stress is a serious problem for a significant proportion of regional home owners. Data compiled by the Mortgage and Finance Association revealed that some 40 per cent of people living in regional Australia were under mortgage stress, compared with about 30 per cent in the city.

Rising house prices and the cost of petrol are squeezing rural family budgets already hit hard by the impact of the drought. Fuel increases have forced up the prices of food, exacerbating the situation in rural areas because it has to be transported long distances

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MORTGAGE STRESS-O-METER: A “scientific approach” to measuring mortgage stress. Graph: aapimage

An Australian Bureau of Statistics breakdown of the 2006 census figures reported that in 2001, when the median family income was about \$49,000, families paying \$1,200 a month in mortgage repayments were under financial stress. Using this median income as the benchmark, the bureau calculated that 290,000 two-parent families with children that year were in mortgage stress.

By 2006, the median family income had risen to \$61,000 so a repayment of \$1,500 a month was said to put people into the mortgage stress category. Taking into account the higher median family income, the bureau estimated 490,000 families

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**STOCK SHOCK:** Falls on the stock market have had a major impact. Photo: aapimage

with children were suffering mortgage stress—almost a 60 per cent hike in the numbers in a mere five years.

The situation is worse for single-parent families. In 2001, the ABS calculated 25,000 such families endured mortgage stress. By 2006, the number had more than doubled to 62,000.

But these calculations were based on the assumption that to endure mortgage stress a person had to spend more than 30 per cent of taxable income on home loan repayments. Fujitsu Consulting's Martin North said this definition is old and misleading.

The company's research revealed that 65 per cent of households spending more than 30 per cent of their income on mortgage repayments were not stressed. So the '30 per cent' rule could result in an over-estimation of the number of households in real mortgage stress and only add to a climate of fear and uncertainty.

North said a single property owner earning \$100,000 a year with no other significant debt yet who spent 40 per cent of the salary on a mortgage would generally not be suffering stress. While this scenario was hardly typical of many Australians, it showed one hard and fast rule did not accurately measure mortgage stress.

To overcome this, North devised what he said was "a scientific approach to truly measure the pulse of Australian home owners, known as the Mortgage Stress-O-Meter". The Stress-O-Meter groups people into one of three categories: no stress, mild stress and severe stress, and within the three categories it can show if a home-owner is at the higher or lower end of each scale.

The system models the financial impact of mortgage stress across 11 discrete segments of the population based on a range of demographic, behavioural and financial factors. The results are then mapped against 26,000 Australian households.

It has to be said, though, that Fujitsu's own calculations are hardly comforting. After all, it is on the basis of his own meter reading that North predicts a million Australians could be suffering some form of mortgage stress by December.

According to North, for every 25 basis-point rise in interest rates, an additional 150,000 households slip into mild stress, and 75,000 move from mild to severe stress. With the bank rate rises this year that situation was already occurring.

"Worryingly, the people in severe stress will have either fallen behind with their payments, are considering selling up, or have had default proceedings commenced against them. A small number of severe stress households would ultimately become bankrupt," North warned.

David Tennant, principal solicitor with the ACT Consumer Law Centre in Canberra, told an Adelaide forum in May that Australia was not having a hangover from the US sub-prime crisis but was undergoing "its own significant consumer credit correction".

Tennant said 'correction' was a polite way of describing what were largely preventable problems driven by a market and regulatory system that "did not care about the consequences of unsustainable activity".

"Ordinary families who were being no more 'unrealistic' than expecting they and their children should be properly clothed and fed are now being squeezed by mistakes for which they are not responsible and over which they have little control," he said.

"The last 10 to 15 years of explosive credit growth and the potential years of pain ahead in returning to sustainable personal debt levels provide more than enough evidence to show that, left alone, the market will not self impose sufficient discipline. Although the current abiding obsession in policy development is deregulation, not learning from and acting on examples of screaming failure is not holding true to values, it is being stubborn."

As it undertakes its inquiry, the House Economics Committee has a crucial task ahead: to assess the effectiveness of competition in the banking and non-banking sectors and to come up with options for improving competition against a backdrop of rate pressures, tighter credit and higher stress. •

For more information on the House of Representatives Economics Committee's inquiry into competition in the banking and non-banking sector, visit [www.aph.gov.au/economics](http://www.aph.gov.au/economics) or email [economics.reps@aph.gov.au](mailto:economics.reps@aph.gov.au) or phone (02) 6277 4587.