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Mr Andrew Gaczol
Acting Secretary
Senate Economics Legislation Committee
Parliament House
Canberra ACT 2600

Dear Mr Gaczol,

National Housing Finance and Investment Corporation Amendment Bill 2019

Genworth welcomes the opportunity to comment on the National Housing Finance and Investment Corporation Amendment Bill 2019 (**Bill**), which is amending the *National Housing Finance and Investment Corporation Act 2018* to enable the establishment of the First Home Loan Deposit Scheme (**Scheme**) on 1 January 2020 by the National Housing Finance and Investment Corporation (**NHFIC**).

Genworth is the leading provider in Australia of lenders mortgage insurance (**LMI**) and is supportive of initiatives that help first home buyers (**FHBs**) make their dream of home ownership a reality sooner. LMI providers including Genworth already help FHBs reduce the size of their home loan deposits and LMI is offered in response to the deposit being such a significant barrier to FHBs being able to enter the housing market in Australia. For the last 54 years, Genworth LMI has been helping Australians with less than a 20% deposit to acquire homes sooner.

The Committee is seeking comment on the effect of the Bill and the Scheme on home ownership, property prices and housing stock. Genworth notes that whilst the Explanatory Memorandum (**EM**) and the second Reading Speech contain some Scheme details in respect of eligibility criteria, termination of the guarantee and regional price caps, the Bill itself goes no further than empowering NHFIC to issue guarantees in favour of FHBs from 1 January 2020. Accordingly, our comments relate to our views on the effect of the Scheme and of the Bill.

Genworth comments as follows:

1. The terms of the Scheme are to be determined by NHFIC under an investment mandate. Without certainty around the 10,000 loan cap, the eligibility criteria, the guarantee termination events, and regional price caps, the potential exists for the Scheme to blow out in size and scope which could be adverse to the tax payer, the banking industry and the LMI industry all who currently support the housing market.
2. While the EM demonstrates the Government's commitment to a healthy, viable LMI industry, it is possible that a future Government may not feel so bound by that commitment and may expand the Scheme and NHFIC's remit at the expense of the supporters of the housing market such as the LMI industry. NHFIC should not be empowered to become a potential taxpayer-subsidised competitor to existing viable, private capitalised LMI providers.
3. In particular, the cap of 10,000 beneficiaries per year may expand the FHB market. Were it to be any bigger, however, we believe the Scheme will just accelerate existing demand, not create any new opportunities for FHBs to enter the market, especially given the current risk appetite in market.

4. Both the Committee (and the Government) should consider whether the proposed eligibility salary caps for Scheme beneficiaries should be lowered to avoid the Scheme being used by people who would simply otherwise use LMI to enter the market at the same time. A more progressive policy approach would be to design the Scheme to target low-to-middle income earners, with the qualifying salary levels determined on a regional basis.
5. The Australian mortgage market is underpinned by borrower recourse. As the Government will be a guarantor to the repayment of 15% of each loan taken out by a Scheme beneficiary it is not clear whether or not NHFIC will pursue borrowers for unpaid monies in the event that they default on their loan and NHFIC is required to pay the lender the arrears.
6. We note that the EM suggests there will be no consumer or lender cost for the guarantee and that NHFIC will not be required to hold capital against each guarantee and potential default. By comparison, the Federal Housing Authority in the United States and Canadian Mortgage Housing Corporation in Canada charge borrowers a fee and are required to retain capital. The lack of a need to maintain capital ultimately means there will be no cash reserves to meet potential NHFIC liabilities arising from mortgage default and any resulting costs will be met by the taxpayer.
7. In its initial media release announcing the Scheme, the Government stated that small lenders will be prioritised to boost competition and that accessibility in regional areas would be a focus of the Scheme eligibility criteria. We do not see any evidence of these promises from the terms of the Bill or the details of the Scheme published to date.

Furthermore, Genworth makes the following additional observations in relation to:

- improvements to the Scheme to deliver a healthy mortgage market; and
- APRA's proposed changes to bank capital standards.

1. Potential improvements to the Scheme that will maintain a healthy mortgage market in Australia

We suggest the following ways to improve the efficacy of the Scheme:

- a) Credit scoring and assessment play an important role in ensuring that creditworthy borrowers are helped with obtaining high loan to value ratio (**HLVR**) loans. By including credit scores in assessing borrowers' eligibility for the Scheme and using them to identify people who have a promising but insufficient credit history (as opposed to poor credit history), the Scheme might be able to help potential FHBs, without either diluting responsible lending practices, or unduly exposing the taxpayers to the risk and cost of loan defaults. There are now three major reputable credit bureaux providing scores in Australia – Equifax, Experian and illion – and they could play an important role in providing a metric that assesses genuine need among FHBs for access to the Scheme in order to buy a home, without “cherry-picking” otherwise “good risks” from the FHB pool that makes the LMI industry sustainable.
- b) In relation to the eligibility criteria, the salary caps for potential Scheme beneficiaries should be set on a sliding salary scale tied to the amount of guarantee together with property price regional caps to limit eligibility/demand to within the 10,000 cap.
- c) To deliver on the small lender and regional competition promise, the eligibility criteria should prioritise access by regional FHBs, and ensure greater involvement by smaller lenders under APRA's Standardised model.
- d) To address the wider issue of housing affordability for FHBs not eligible to benefit under the Scheme, the Commonwealth should treat the fee that a borrower effectively pays their lender for the lender's LMI premium as tax deductible, on a sliding scale for owner-occupier FHBs. Given that the Scheme will be capped at 10,000 beneficiaries a year, this would enable more FHBs to benefit from the Government's commitment to supporting a broader group of FHBs within reasonable, progressive parameters.

2. Consideration of APRA's discussion paper on changes to APS 112 and 113 – changes to the Standardised and Internal Ratings Based (IRB) models for banking capital

Running concurrently with the Scheme proposal consultation is the consultation by APRA on possible changes to the Basel III capital framework, with potential implications for LMIs¹. The Australian LMI market has experienced significant headwinds since the implementation of Basel II in Australia since 2008, as those reforms effectively created a disincentive to the larger, more sophisticated Internal Ratings Based (IRB) mortgage lenders from using LMI². LMI is a very well capitalised industry, at 1.6 times APRA's prescribed amount.³

To address this, the LMI industry has been urging APRA to leave the current Basel II risk weight penalties for no LMI by loan to value (LVR) band in place, and that for the larger lenders, there should be a 30% reduction in either Loss Given Default (LGD) or total risk weighting.

If APRA dilutes the incentive for smaller (or Standardised) lenders to use LMI through changes to the risk weights, it will make it harder for them to compete with larger lenders in the high LVR lending space. Standardised lenders help to create competition, offer products to niche markets and create product choice for consumers.

Obviously, APRA's independence from Government is important and well understood, but the weight of parliamentary support for recognising the value of LMI in APRA's banking capital framework would do much to help ease the tension between the high standard of APRA's responsible lending guidelines, which the LMI industry has worked hard to support, and the relaxation of controls on FHBs entering the market, as proposed by the Scheme. It will be a significant burden on the LMI industry to try and cope with competing interests at both ends of the regulatory spectrum.


Conclusion

Genworth appreciates this opportunity to make comment on the Bill and the Scheme. We are equally committed as the government to securing the future of FHBs and helping Australians realise the goal of responsibly buying their first home by significantly reducing the time it takes them to save a 20% deposit.

Genworth shares, with all Australian taxpayers, the need for the Scheme to be established in such a way that it supports and complements the existing viable and effective LMI industry and also complements a full range of policy options proposed to help FHBs access the Australian housing market sooner and in a responsible way.

My colleagues and I would appreciate the opportunity to discuss our comments with the Committee, at a mutually convenient time. I look forward to hearing from you soon.

Yours sincerely,



Georgette Nicholas
Chief Executive Officer and Managing Director

¹ Available here: <https://www.apra.gov.au/consultations-revisions-capital-framework-authorised-deposit-taking-institutions>

² As of September 2019, these are deemed by APRA to be ANZ, CBA, NAB, Westpac, Macquarie and ING.

³ Source: <https://www.rba.gov.au/publications/fsr/2018/oct/aus-fin-sys.html>