Regulation impact statement – Home Guarantee Scheme

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Executive summary

For many Australians seeking to enter the housing market, the most significant barrier has become the time it takes to save a sufficient deposit, rather than the ability to service a mortgage. For those wishing to purchase in the near term but are yet to save a sufficient deposit, a private market solution exists in the form of lenders mortgage insurance (LMI). However, LMI adds to the cost of borrowing and can delay access to home ownership for some including first homebuyers, single parents with dependants, older Australians and people living in regional Australia. Moreover, some cohorts of homebuyers are significantly less likely to have the financial capability to enter the housing market even with the provision of LMI.

The expansion of the Home Guarantee Scheme is designed to support earlier access to home ownership for cohorts that may otherwise struggle to gain a foothold in the market in the near term. It builds upon the Commonwealth Government's existing guarantee programs which allow applicants to purchase a home with a deposit of as low as 2 per cent, without the need for LMI.

Since the establishment of the First Home Loan Deposit Scheme (FHLDS), stakeholders have expressed broad support of the Scheme and its objective to assist Australians into home ownership. The expansion of the Home Guarantee Scheme seeks to extend this support to target cohorts.

The need for Australians to invest in their own home is important. For many Australians, home ownership also provides significant social benefits in addition to economic and financial benefits. An increase in places will be required to ensure this goal is achieved.

A key indicator of whether the Scheme has achieved its objectives will be whether it is able to operate alongside a viable and profitable LMI sector that continues to support other first home buyers' access to the market. Maintaining the viability of the LMI industry is imperative, as it allows potential home buyers that don't qualify for the Scheme to enter the property market sooner than they would otherwise would.

The Office of Best Practice Regulation's (OBPR's) assessment (22-01418) was that the quality of the analysis in the RIS was good practice and therefore sufficient to inform a decision.

1. What is the problem you are trying to solve?

The Home Guarantee Scheme supports earlier access to home ownership for cohorts that may otherwise struggle to gain a foothold in the market in the near term – particularly first homebuyers, single parents with dependants and older Australians, while also driving jobs in the residential construction sector. It recognises that for many Australians seeking to enter the housing market, the most significant barrier has become the time it takes to save a sufficient deposit, rather than the ability to service a mortgage. For those wishing to purchase in the near term but that have yet to save a sufficient deposit, a private market solution does exist, in the form of lenders mortgage insurance (LMI). However, LMI can add significantly to the cost of borrowing and this additional cost can delay access to home ownership for some. Furthermore, some cohorts of homebuyers are significantly less likely to have the financial capability to enter the housing market even with the provision of LMI, meaning that a private market solution does not exist for all potential homebuyers.

The Home Guarantee Scheme builds on the Commonwealth Government's existing guarantee programs to support earlier access to home ownership. The FHDLS, which began on 1 January 2020, allows first home buyers to buy a home with a deposit as low as 5 per cent without needing to pay LMI. This scheme has been very successful with practically all the 10,000 places in each financial year being taken up in the first few months of being made available. The New Home Guarantee, which allows for the construction of a new home (or the purchase of a newly built home) with a minimum deposit of 5 per cent without LMI, has supported more than 8,000 first home buyers over the past two financial years. Most recently, the Family Home Guarantee, which supports single parents with dependants to purchase a home with a deposit of as low as 2 per cent, has been taken up by more 1,600 people in the first few months of operation.

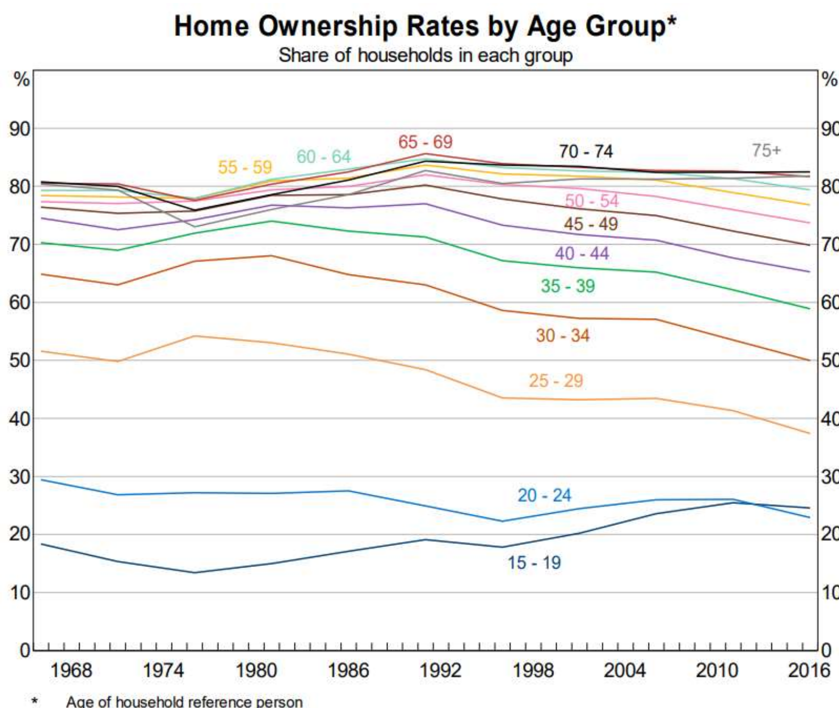
The strength of demand for these existing guarantee programs points to ongoing pressure on the ability of first home buyers (and single parent families) to be able to access the "Australian dream" of home ownership. Home ownership is an important pillar of Australian society, with research indicating that home ownership provides a foundation for family and social stability and contributes to improved health and educational outcomes and a productive workforce.[1]

In addition to the social benefits, home ownership generally confers significant economic and financial benefits on Australians. The Retirement Income Review found that "the home is the most important component of voluntary savings and is an important factor influencing retirement outcomes and how people feel about retirement. Retiree homeowners generally have lower housing costs and an asset that can be drawn on in retirement"[2], which generally translates into lower dependence on Government support in retirement. While retiree renters can access Commonwealth Rent Assistance to offset their housing costs, it is often far below the level that would bridge the gap in living standards compared to homeowners.[3]

While home ownership is an aspiration for most Australians, it has become more challenging for people to enter the property market. The rate of home ownership in Australia has been

[1] Productivity Commission (2004), First Home Ownership - Productivity Commission Inquiry Report.
[2] Treasury (2020), Retirement Income Review, page 18 and page 137
[3] Treasury (2020), Retirement Income Review, page 54

falling in recent decades. The proportion of households that own a home has fallen to 66 per cent, down from 70 per cent in 1997-98.[4] Home ownership rates have fallen across most age groups since the early 1990s and this trend is most evident among households aged 25 to 49. Concurrently, the number of households renting has increased from approximately one quarter in the late 1990s to over one third in 2018.[5]

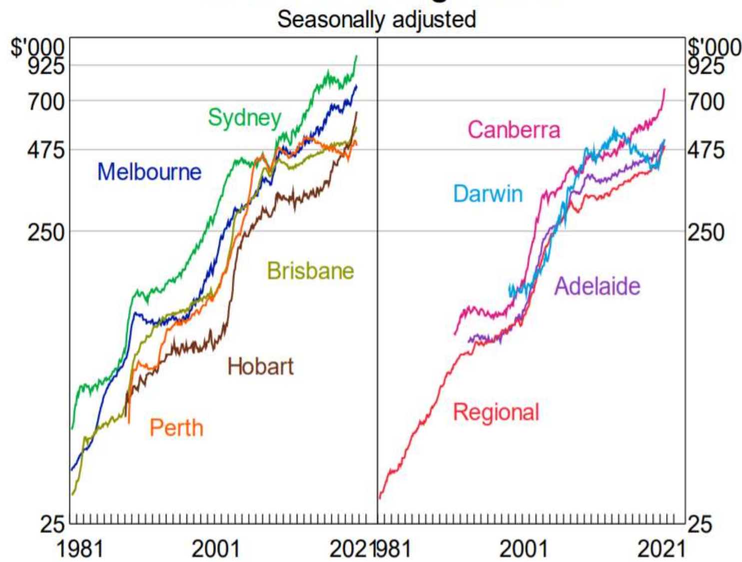


Source: RBA

House prices have risen substantially over the past year, from already high levels. National house prices have risen by 22.4 percent over the year to January 2022 with both cities and regional areas experiencing strong price growth. Many factors have been cited for this most recent increase, including the very low interest rate environment, a generally better-than-expected economic recovery from the pandemic, changes in preferences, and the range of stimulus programs put in place by both the Commonwealth and state and territory governments during the pandemic.

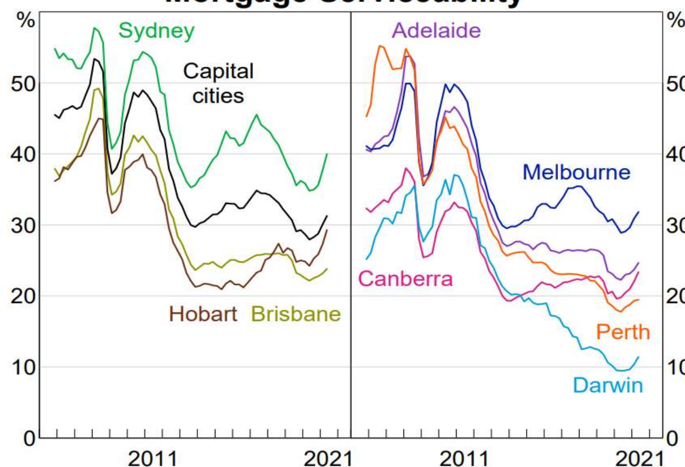
[4] Australian Bureau of Statistics (2019), More households renting as home ownership falls.

[5] Reserve Bank of Australia (RBA), *Submission to the Inquiry into Housing Affordability and Supply in Australia*, Australian Parliament House website, Accessed 20/10/2021. https://www.aph.gov.au/Parliamentary_Business/Committees/House/Tax_and_Revenue/Housing affordability/Submissions



Data on house prices alone however is insufficient to accurately assess the evolution of housing affordability. A commonly cited measure of housing affordability is the ratio of house prices to household incomes. This measure has increased steadily since the early 1980s and has increased particularly rapidly over recent years, rising to an all-time high. Higher house prices relative to income means that, in the absence of other factors, the average home buyer must save for longer to be able to afford a deposit on a home and would need to make higher loan repayments as a proportion of income to service the mortgage.

While the ratio of house prices to incomes has risen sharply, mortgage serviceability has generally improved over recent years. Mortgage serviceability measures the cost of meeting mortgage repayments as a proportion of household income. The substantial decline in interest rates over the past few years has lowered the cost of servicing a typical mortgage, however, the sharp price rises more recently have led to a renewed deterioration in serviceability.

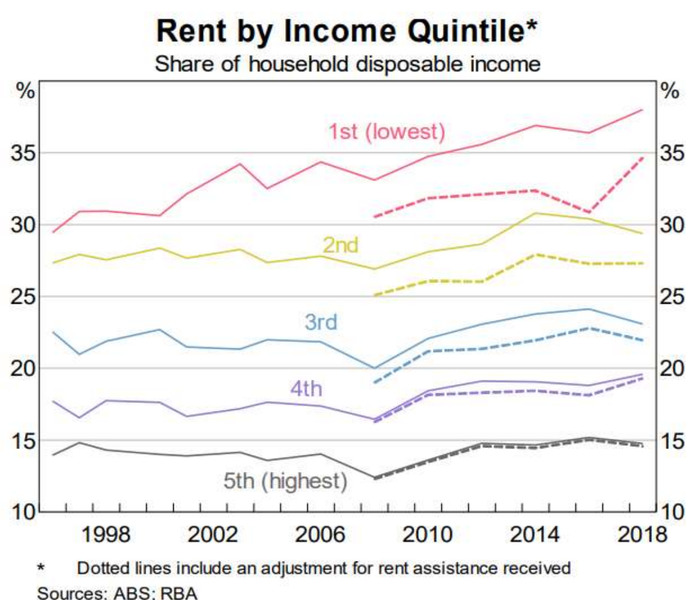


Source: RBA

Nevertheless, the biggest constraint on housing affordability has become the time it takes to save a sufficient deposit, rather than the ability to service a mortgage. As a share of income, the average first home buyer deposit has risen significantly in recent years, from below 70 per cent of average annual household income in 2010 to over 80 per cent in 2021.[6] Consequently, the average time it takes the average first home buyer in capital cities to save a deposit has increased by approximately 25 per cent over the past decade.[7] For many prospective buyers, it takes approximately 10.7 years in capital cities and 9.1 years in regional areas to save for a deposit.[8]

The RBA has found that higher prices and specifically higher deposit hurdles for new home buyers explain the majority of the variation in first home buyer activity over the past few decades. The aforementioned data shows the increase in house prices and their consequential effects on increasing the deposit requirement to enter the property market. This clearly points to the need to address the deposit hurdle for those who are seeking to enter the property market but that do not have a sufficiently high income to save enough for a sizeable deposit, especially when renting at the same time.

High rental costs are also contributing to the difficulty in saving for a sufficient deposit to purchase a home. Over the past decade, rent as a share of household income has risen significantly. Even after adjusting for rent assistance received, households in the lowest income quintile have experienced the most significant increase in rental costs.[9] This places increasing pressure on lower-income households to save enough income for a deposit while enduring the rising income burden of rental costs.



6 RBA
7 RBA
8 ANZ, 2021
9 RBA

2. Why is Government action needed?

The Home Guarantee Scheme assists cohorts of people who face barriers to home ownership owing to high deposit requirements, but are able to meet mortgage serviceability requirements. It should be noted, however, that although the challenge of saving a sufficient deposit is most evidently faced by first home buyers (who typically tend to be younger), the challenge can be just as great for some older Australians, including those who may have previously owned a home.

A private market solution does exist through lenders mortgage insurance (LMI). However, it only partially addresses the problem due to the additional costs it imposes on homebuyers, thereby impacting on affordability. For potential first home buyers seeking to purchase in the near term but that have yet to save a sufficient deposit, commercial lenders will typically require the borrower to purchase LMI. LMI is a form of credit protection insurance that protects a lender from losses in the event of a borrower defaulting on a home loan. Lenders choose whether to purchase LMI when extending credit to borrower, and typically do so if the loan exceeds more than 80 per cent of the value of the property.

LMI is a somewhat peculiar insurance product. While it protects lenders from the risk of financial loss, the cost of the LMI premium is typically paid by the borrower. Moreover, while an LMI contract protects the lender from losses over the life of the mortgage, the premiums are generally paid upfront as a lump sum, rather than in regular periodic payments over the life of the contract (as occurs with most insurance products).[10]

As such, LMI can add significantly to the overall cost of purchasing a home. For a first home buyer purchasing a $700,000 property with a 5 per cent ($35,000) deposit, the typical upfront LMI premium would be almost $28,000.[11] Where an upfront LMI premium is charged, borrowers typically capitalise the premium into their loan amount (i.e. their overall borrowing requirement increases by the size of the LMI premium), which will tend to increase the total amount of interest paid by the borrower. Using the scenario above, if the borrower were to capitalise the LMI premium into the loan and pay down the loan on schedule over a 30-year term, it would increase total repayments by $51,074, including interest charges of $23,074[12].

For prospective home buyers on modest incomes, the additional cost associated with an LMI-supported purchase can be enough to put that purchase out of reach. For some, this may mean saving for a larger deposit over a more extended period to avoid the need to pay LMI altogether, or simply to reduce how much LMI they will have to pay (the size of the LMI premium is mostly a function of the loan-to-valuation ratio).

Stakeholder consultation conducted during the recent Statutory Review of the Operation of the *National Housing Finance and Investment Corporation Act 2018* (the NHFIC Review) indicated that the majority of successful applicants to the FHLDS to date can be

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[10] Note that one provider of LMI in Australia has recently offered a new product that gives the borrower the option to pay the premium in regular instalments.

[11] Based on a 30-year mortgage term for an owner occupier, excluding stamp duty (https://www.genworth.com.au/products/tools/lmi-fee-estimator).

[12] Based on an interest rate of 4.50 per cent, a 30 year loan, a monthly repayment frequency, a monthly fee of $10 and using the moneysmart.gov.au loan calculator.

characterised as ‘accelerated buyers’ – those who would have been able to purchase a property, either with the support of LMI or with a 20 per cent deposit, within one or two years. An LMI provider submitted to the NHFIC Review evidence that the FHLDS is also assisting a proportion of first home buyers that may not have otherwise been able to enter the market – ‘genuinely additional buyers’. The submission observed that approximately 12 per cent of successful FHLDS applicants had income levels lower than those that would generally be acceptable for non-scheme loans.

Data compiled by NHFIC from participating lenders, found that the average income of applicants under the FHLDS over the 2020-21 financial year was $69,167 for singles and $115,023 for couples. These averages are appreciably below the income caps that apply under the FHLDS ($125,000 for singles and $200,000 for couples) and suggest that the FHLDS may be genuinely helping those for whom the additional impost of LMI would be a significant barrier to their ability to enter the market.

The public provision of mortgage insurance as a means to assist low to moderate-income earners obtain housing finance is relatively common overseas. Indeed, Australia is relatively unique in having an active private market for LMI, at least since 1997 (when the Commonwealth Government’s Housing Loans Insurance Corporation was privatised).[13] For a summary of international examples where governments support the provision of LMI, see Box 13.2 from the Productivity Commission’s Inquiry into Competition in the Australian Financial System (reproduced below):

[13] Productivity Commission Inquiry into Competition in the Australian Financial System, June 2018, p369.

Box 13.2 **Internationally, governments often support the provision of LMI**

In **Canada**, mortgage insurance is provided by three institutions: the Canada Mortgage and Housing Corporation (CMHC) (state-owned), Genworth (privately owned) and Canada Guaranty (privately owned). The Government backs 100% of the mortgage insurance obligations of CMHC and 90% of the private insurers' obligations (lenders are expected to meet 10%) (Londerville 2010). The Government guarantee is intended to support access to home ownership for creditworthy buyers and promote stability in the housing market, financial system and economy (DoF (CA) 2016).

In **Hong Kong**, mortgage insurance has been provided by Hong Kong Mortgage Corporation Insurance Ltd, which is wholly-owned by the Hong Kong Government, since 1999. The objectives of the program are to promote home ownership and maintain banking stability (HKMC 2018). Private mortgage insurers (including Arch MI Asia and QBE Asia) also operate in the Hong Kong mortgage insurance market.

In the **Netherlands**, mortgage insurance is administered by the Homeowner Guarantee Fund and backed by a government guarantee, the *Nationale Hypotheek Garantie* (NHG). The NHG is available for mortgages on properties with a maximum value of EUR 245 000 (A$390 000). Mortgages guaranteed by the NHG must meet the criteria for responsible lending and borrowing set by the Netherlands National Institute for Family Finance (NHG (NL) 2017). In 2016, 73% of the housing stock had been bought by private individuals under the price ceiling and financed with an NHG-backed mortgage. However, the share of new mortgages backed by the NHG has been declining as the property value cap has not kept pace with rising house prices.

In the **United Kingdom**, the Government operated a 'help to buy' mortgage guarantee scheme from October 2013 to June 2017. The scheme offered lenders the option to purchase a guarantee on mortgage loans where the borrower had a deposit of 5% to 20%, and was limited to owner-occupied homes with a maximum value of £600 000 ($A1.09m). The guarantee compensated participating mortgage lenders for 95% of net losses suffered in the event of a repossession, down to 80% of the purchase value. Ten lenders participated in the scheme, covering 2.7% of all residential mortgage completions in the UK over that period (HMT (UK) 2017).

In the **United States**, there is a mixed market for mortgage insurance, with the Federal Housing Administration, the Department of Agriculture and the Department of Veterans Affairs having 65% of the market and six private insurers sharing the remaining 35%. The main driver of LMI is the requirement on Fannie Mae and Freddie Mac, the government-sponsored enterprises, to obtain credit enhancement for mortgages with LVRs above 80% (Goodman and Kaul 2017). The federal agencies and private insurers have different conditions and pricing for mortgage insurance.

Through the operation of the FHLDS and, subsequently, the New Home Guarantee and the Family Home Guarantee, the Commonwealth has demonstrated it has the capacity to intervene successfully to support home ownership for those who are able to secure one of the limited number of guarantee places made available under these programs.

As alluded to above, demand for guarantee places in these programs – particularly the FHLDS – has outstripped the available supply. The FHLDS is currently capped at 10,000 guarantees each financial year, and the majority of each financial year's guarantees have been exhausted within the first few months of being made available. Demand for the New Home Guarantee places from first homebuyers has also been strong. While only around half of the available guarantees in 2020-21 were taken up, this reflects, in part, transient factors associated with material and labour shortages in the residential construction industry. The Government has announced that up to 10,000 Family Home Guarantee places will be made

available over the four years from 2021-22, and more than 1,600 of those available places have already been taken.

Despite the high level of demand across all the programs, key lending indicators of the FHLDS and associated extensions show that guarantee backed loans are performing well. As at 30 June 2021, 33,000 guarantees had been issued. Of these, no scheme-backed loans had defaulted.[14] Further, through a combination of reduced interest rates and increased savings during the COVID-19 pandemic, mortgage repayments as a share of income dropped for scheme-backed loans fell from a median of 24.5 per cent in 2020-21 to 23 per cent in 2021-22.[14]

Clearly, demand from those seeking to enter the housing market could support an expanded Home Guarantee Scheme. A question that naturally arises is how far should such intervention go? One of the Government's stated design objectives for the FHLDS (and the New Home Guarantee and Family Home Guarantee) is for the scheme to operate alongside a viable and sustainable private market for LMI.

Because of the role that LMI plays in supporting home ownership generally, consultations during the NHFIC Review argued that failure in the private LMI market could adversely impact home ownership. The withdrawal of one or more private LMI providers from Australia could lead to pressure for Government support on a much larger scale. A scenario under which the Commonwealth effectively displaces a large portion of the mortgage insurance sector would represent a transfer of that risk from the private to public sector.

Given this, an informed understanding of the capacity of the LMI sector to accommodate the Government's intervention in the market should continue to be a key input into any consideration of changes to the scheme, including any consideration of an expansion in its size or scope.

Capacity of the LMI sector to accommodate an expanded Home Guarantee Scheme

The FHLDS is supporting 10,000 first home purchases a year. The New Home Guarantee is supporting another 10,000 first home purchases in 2021-22 and the Family Home Guarantee will support up to 10,000 guarantees in total over four years from 2021-22. Even when aggregated, this is a relatively small proportion of the total first home buyer market each year (typically just over 100,000 per year)[15] and an even smaller proportion of the average of 465,000 property transfers every year.

Data from APRA's quarterly general insurance statistics indicates that approximately 179,000 new loans were underwritten by LMI providers in 2020-21. The current guarantee schemes therefore represent a relatively small share of what would be covered by the LMI sector (assuming all scheme places are taken up and all would have otherwise used LMI).

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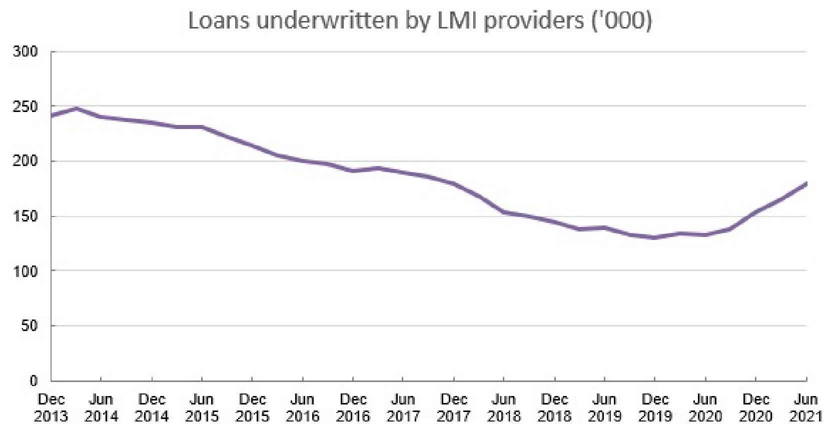
[14] First Home Loan Deposit Scheme and New Home Guarantee Trends & Insights Report 2020–21

[15] To note, the Family Home Guarantee is not limited to first home buyers.



Source: APRA

On the evidence available, it is likely that a proportion of the FHLDS and NHG guarantee places issued under these schemes could displace business that otherwise would have gone to the LMI sector. Using the estimate cited above, approximately 12 per cent of successful FHLDS applicants had income levels lower than what would generally be acceptable for non-scheme loans, meaning 88 per cent of scheme supported loans could have been eligible for LMI. As such, on the current size of the guarantee programs (in aggregate, around 22,500 each financial year), we estimate the Home Guarantee Scheme could represent around 15 per cent of the average number of loans supported by LMI each year.

In contrast, the Family Home Guarantee and the proposed Mature Home Guarantee, represent cohorts that are significantly less likely to have the financial capability to enter the housing market. For these cohorts, a far greater percentage would likely be ineligible for a non-scheme loan with LMI, with many instead remaining long-term renters, including in the social and affordable housing sector. Consequently, these cohorts gaining access to scheme places are less likely to negatively impact the LMI sector, as they would have been unlikely to have used it.

However, across each of the schemes, just because a recipient is eligible for a non-scheme loan using LMI, does not mean they would have used it. Some borrowers may have simply waited until they had a sufficient deposit, not enter the housing market at all, or pursued alternative forms of financing their deposit, such as a borrowing from their relatives.

Previous consultations with LMI providers, including through the NHFIC Review, have suggested that it is difficult to determine the full impact of these schemes on the LMI sector at this point in time. Because the schemes mostly bring forward demand from future years it will likely take some time to flow through on LMI providers' business. Moreover, the past two years have been seen unprecedented and exceptional economic circumstances brought about by the COVID-19 pandemic and the sector has benefited from much stronger than expected cyclical conditions in the housing market.

From a prudential perspective the LMI sector is robust. APRA conducted several stress test exercises with four active lenders mortgage insurers in the second half of 2020.[16] The results of these stress tests indicate that they are well-positioned to withstand a very severe economic downturn. Specifically, the results indicate that despite significant losses of capital under a severe economic downturn, the LMI industry as a whole remained above their minimum capital requirements, while still meeting their commitments to policyholders. However, APRA did find that the resilience of some LMIs was challenged under the severe downturn scenarios (where there are very high mortgage default rates due to a significant economic shock), with some insurers falling below their minimum capital requirements before using management actions to respond to the stress.

Commercially, the LMI sector has recovered quickly from the impact of the COVID-19 downturn. Loss provisions made early in the pandemic proved to be overly pessimistic, as Australia's unemployment rate and housing prices, two variables closely linked to LMI claims, improved more quickly than anticipated by insurers. Likewise, rising house prices have driven higher LMI premiums, which has supported underwriting revenue. The strong recovery following the impact of COVID-19 can be seen in the recent performance of Genworth, one of the largest LMI providers in the country. Genworth has seen a sustained increase in number of premiums underwritten in the first half of 2021 and has reported a net profit of $76.4 million as of 30 June 2021.

While prudentially the Australian LMI sector is robust and currently profitable, there remains a risk that independent LMI providers could leave the market based on their assessment of long-term commercial viability. This will depend on both the impact of government policy and the economic outlook, including house prices. Nevertheless, events over the past year indicate that the Australian LMI sector remains attractive to investors. For instance, Genworth LMI was sold off from its US parent company to a diverse range of institutional investors, and likewise, Arch, recently purchased Westpac LMI.

Potential impact on the housing market and house prices of an expanded Home Guarantee Scheme

While there is no direct cash payment involved, the Home Guarantee Scheme effectively operates to increase the purchasing capacity of qualified prospective buyers, akin to the more widely used first home buyer grants. By way of example, for a first home buyer purchasing a $500,000 home with a $25,000 deposit (five per cent), the typical LMI premium would be around $14,800. If the need to obtain LMI is removed, this $14,800 can theoretically be added to the buyer's spending capacity, meaning that their budget for a home might be increased by $14,800.

Policies that increase the purchasing capacity of buyers can have the effect of pushing up house prices. Assistance to first home buyers that simply brings forward or adds to demand without a corresponding increase in supply is likely to result in an increase in house prices which largely cancels out any positive benefit to first home buyers (with most of the benefits

[16] APRA, Stress testing insurers during COVID-19: results and key learnings.

ultimately accruing to vendors – those who already own property or to developers and builders of property).

It is difficult to isolate the impact of this relatively small scheme from the impact of other government initiatives (such as the HomeBuilder program, the First Home Super Saver Scheme, first homeowner grants, and various state and territory stamp duty exemptions and discounts) and within the context of broader macro and micro influences on the housing market. However, the targeted nature of the program and the limits on the number of guarantees per year suggests the aggregate impact on prices is very modest.

3. What policy options are you considering?

Three policy options are considered:

- **Option 1**: The status quo (no change to the existing guarantee schemes).
- **Option 2**: Increasing the annual allocation of places for first home buyers, a new Regional Home Guarantee and Mature Home Guarantee, with a total of 50,000 guarantee places available each year.
- **Option 3**: As per Option 2, however where the total number of guarantees available each year is limited to 30,000 places.

In addition, section 5 discusses policy options raised by stakeholders and how these have been incorporated into decision making.

Option 1

Under Option 1, the existing schemes would continue to operate as below:

Name	**Cohort**	**Income cap Single/Couple**	**Price Cap** (To be reviewed for 1 July 2022)	**Property type**	**Minimum deposit**	**Number of Guarantees**	**Major/Non-major lender split**
First Home Loan Deposit Scheme (FHLDS)	First home buyers	$125k/$200k	Existing	New & established	5 per cent	10,000 per annum, ongoing	50 per cent of guarantees reserved for non-major bank lenders
Family Home Guarantee	Single parents	$125k	Existing	New & established	2 per cent	10,000 over four years from 2021-22	No restriction
New Home Guarantee	First home buyers	$125k/$200k	Existing	New only	5 per cent	10,000 in 2021-22	50 per cent of guarantees reserved for non-major bank lenders

Option 2

Expand the existing schemes including:

- an increased annual allocation of 30,000 places for first home buyers under a rebranded FHLDS (the First Home Guarantee); and
- a new Regional Home Guarantee and Mature Home Guarantee that would operate with the existing New Home Guarantee and Family Home Guarantees terminating in 2024-25, with a total available pool of 20,000 guarantee places each year.

The Home Guarantee Scheme would operate as below:

Name	**Cohort**	**Income cap Single/Couple**	**Price Cap** (To be reviewed for 1 July 2022)	**Property type**	**Minimum deposit**	**Number of Guarantees per FY**[17]	**Major/Non-major lender split**
First Home Guarantee (FHG) (rebrand of FHLDS)	First home buyers (FHBs)	$125k/$200k	Existing	New & established	5 per cent	30,000 (rollover possible into next FY)	50 per cent of guarantees to be reserved for non-major bank lenders
Family Home Guarantee	Single parents	$125k	Consistent with FHG	New & established	2 per cent	No individual caps, subject to overall cap of 20,000 across all four guarantees (rollover possible into next FY non-FHG pool)	No restrictions
New Home Guarantee	FHBs	$125k/$200k	Existing, higher than FHG	New only	5 per cent		
Regional Home Guarantee	FHBs and Non-FHBs in regional areas, including regional centres	$125k/$200k	Consistent with NHG	New only and for homes in in regional areas	5 per cent		
Mature Home Guarantee	FHBs and Non-FHBs aged 50 years and over	$125k/$200k (relaxed couple / partner requirements)	Consistent with FHG	New & established	5 per cent		

[17] Unused guarantees from each financial year will be eligible for roll over into the subsequent financial year, with FHG places rolling over into a FHG pool and places from the other four guarantees rolling over into a separate, combined pool.

All other policy design parameters, such as the operation of the guarantee, treatment of construction loans, administrative mechanisms and participating panel of lenders will remain the same, as outlined in the *National Housing Finance and Investment Corporation Investment Mandate Direction 2018* (the Investment Mandate).

Option 3

As per option 2, but caps the total available guarantee places to 30,000 each year. The First Home Guarantee would be capped at 20,000 places per year while the remaining pool would be capped at 10,000 per year.

Name	**Cohort**	**Income cap Single/Couple**	**Price Cap** (To be reviewed for 1 July 2022)	**Property type**	**Minimum deposit**	**Number of Guarantees per FY**[18]	**Major/Non-major lender split**
First Home Guarantee (FHG) (rebrand of FHLDS)	First home buyers (FHBs)	$125k/$200k	Existing	New & established	5 per cent	20,000 (rollover possible into next FY)	50 per cent of guarantees to be reserved for non-major bank lenders
Family Home Guarantee	Single parents	$125k	Consistent with FHG	New & established	2 per cent	No individual caps, subject to overall cap of 10,000 across all four guarantees (rollover possible into next FY non-FHG pool)	No restrictions
New Home Guarantee	FHBs	$125k/$200k	Existing, higher than FHG	New only	5 per cent		
Regional Home Guarantee	FHBs and Non-FHBs in regional areas, including regional centres	$125k/$200k	Consistent with NHG	New only and for homes in in regional areas	5 per cent		
Mature Home Guarantee	FHBs and Non-FHBs aged 50 years and over	$125k/$200k (relaxed couple / partner requirements)	Consistent with FHG	New & established	5 per cent		

[18] Unused guarantees from each financial year will be eligible for roll over into the subsequent financial year, with FHG places rolling over into a FHG pool and places from the other four guarantees rolling over into a separate, combined pool.

4. What is the likely net benefit of each option?

Option 1

Under the status quo option, the existing guarantee schemes would support a path into home ownership for around 22,500 individuals or couples in the 2021-22 financial year, falling to around 12,500 in subsequent financial years upon expiry of the temporary New Home Guarantee.

This would continue to represent a relatively small share of annual first home buyer activity and a small share of overall mortgage lending. As such the associated impact on dwelling prices (at least at the aggregate level) and activity in the residential property market is likely to remain relatively minimal. At such a small scale, there is a high likelihood the guarantee schemes would continue to operate alongside a viable and sustainable private LMI sector. There are no additional regulatory costs or savings associated with this option.

While mortgage serviceability remains low, the rate of house price appreciation over the past year in particular has further increased the required deposit for prospective homeowners. Without additional government support to shorten the time taken to save for a deposit, it will take longer for people to enter home ownership or require people to pay more with LMI.

Option 2

Option 2 entertains an increase in the size and scope of the Government's policy intervention. The option would increase the total number of guarantees available each financial year to 50,000, from around 22,500 available in the current financial year. Further, the introduction of the Regional Home Guarantee and Mature Home Guarantee would expand the scope of the existing guarantee programs to include the additional cohorts of non-first home buyers in regional areas and older non-first home buyers.

This would provide support to a larger number of Australians seeking to enter the housing market. The associated impact on dwelling prices and activity in the residential property market is likely to be more significant. As discussed above, the available evidence indicates that the FHLDS (and New Home Guarantee) has mostly had the effect of bringing forward demand that would have otherwise occurred over the next one to two years. Gauging the impact on dwelling prices is inherently challenging given the difficulty in disaggregating the numerous competing forces exerted on the housing market (for example, population growth, interest rates, housing supply, consumer preferences, household incomes, economic activity, and government support), however a bring forward may have an impact on aggregate dwelling prices and the pattern of market activity.

As discussed in section 2, the bring forward of demand for home buyers utilising the HGS can impact house prices. This is because, in the absence of a supply response, increased demand will elicit a price response. However, the impact on house prices from the HGS is expected to be, at most, modest. The NHFIC Review was not able to determine if the existing FHLDS has had any significant price impact and notes that the scheme is small in size in the context of the overall housing market. Even a doubling of guaranteed places available would not represent a very large portion of the total number property transactions each year (approximately 465,000 per year). Furthermore, the effects of other drivers of

housing prices cannot be disaggregated from that of a scheme which only supports a relatively small number of property purchases.

As discussed in section 2, evidence presented to the NHFIC Review indicates that around 88 per cent of successful FHLDS applicants could have been eligible for LMI. Assuming that the entirety of these eligible applicants access the HGS rather than LMI, an increase in the number of guarantees available to 50,000 per year could represent around 25 per cent of the average number of loans supported by LMI each year. It is important to note, however, that the Family Home Guarantee and the proposed Mature Home Guarantee supports cohorts that are significantly less likely to be able to enter the housing market even with the support of traditional LMI products.

Moreover, while an expanded HGS could represent around 25 per cent of the *number* of LMI-supported loans each year, the property price caps for the HGS mean that the average loan size for scheme-supported loans is likely to be lower than the average loan size for LMI-supported loans. For a given Loan-to-value ratio (LVR), LMI premiums are typically charged as an increasing function of the loan size. As such, the expected impact on LMI sector revenues is likely to be less than is implied by simply comparing the number of scheme-supported loans to the number of LMI-supported loans in a given year. For example, a 95 per cent LVR loan to purchase a property with a value of $1,000,000 (above the highest property price cap) would attract an LMI premium of just over $44,000. By contrast, a 95 per cent LVR loan to purchase a property with a value of $500,000 would attract an LMI premium of just under $15,000.[19]

The analysis presented above suggests the LMI sector should be able to accommodate an expansion in the size of the Government's guarantee programs. Nevertheless, there remains a risk that further Government expansion into the mortgage insurance sector impacts the sector's profitability to the extent that a LMI market participant exits the market. In that eventuality, the price of LMI contracts may increase and/or some lenders may instead increase the price of loans for high LVR lending as a substitute for an LMI policy (some lenders already do this for loans with a LVR of up to 85 per cent). This risk should be assessed in the context of the current financial strength of the LMI market which has robust prudential standards and increasing profitability.

Borrowers entering the housing market (both those supported by the HGS and those who are not) are exposed to the possibility of a decline in prices, an increase in repayments and/or a change in personal circumstances (including a reduction in household income). An important mitigant to this risk is the existing responsible lending obligations on providers of credit and the prudential standards that apply to authorised deposit-taking institutions. Commercial lenders must satisfy themselves that the borrower is able to make home loan repayments in a wide variety of scenarios, including an increase in interest rates, regardless of the source of their deposit or whether their loan is backed by some form of guarantee or insurance cover. This indicates the risks stemming from borrowers supported by the HGS

[19] Based on a 30-year mortgage term for an owner occupier, excluding stamp duty. See: https://www.genworth.com.au/products/tools/lmi-fee-estimator.

can be expected to be no greater than for those who choose to enter the market through an LMI-supported loan.

Although the HGS does not involve Government cash payments, the guarantees represent a liability for the Government in the event of a default, if there is a shortfall between the property sale price and the loan outstanding. The current FHLDS scheme has not experienced any defaults to date and the number of distressed loans (in arrears) is extremely low. Based on the experience of the existing scheme, the thorough assessment that lenders must undertake on potential borrowers and that the broad parameters of the HGS remain the same, the expanded scheme is not expected to result in a significantly higher rate of default than the current FHLDS scheme and is very unlikely to represent a significant financial risk to the Commonwealth.

Infrastructure associated with the existing guarantee programs is easily scalable to accommodate the increased allocation of guarantees, so that additional regulatory and administrative burden on NHFIC and panel lenders is likely to be minimal. Further, applications to the guarantee schemes are built into loan applications and would not significantly increase time involved for applicants.

Methodology used to estimate regulatory costs to individuals – Option 2

Under Option 2, regulatory costs to individuals come from the additional time it takes individuals to understand the requirements of the guarantee schemes.

Based on the range of industry estimates gathered through desktop research, the following assumptions were made to determine the regulatory costs to individuals under Option 2:

- An increase in available guarantee places each year as outlined in section 3 above.
- Individuals spend 1 additional hour to understand the requirements of the guarantee schemes.
- Using the Office of Best Practice Regulation estimate for individual costs at $32.00 per hour.

The total estimated average regulatory costs to individuals under Option 2 is $0.808 million per year.

Methodology used to estimate regulatory costs to lenders and brokers – Option 2

Under Option 2, regulatory costs to lenders and brokers come from the additional time it takes to educate front-line lenders and brokers on the requirements of the new guarantee schemes, system updates, ongoing administrative costs to lenders through processing additional loans, and costs associated with processing estimated defaults on additional loans.

The following assumptions were made to estimate the regulatory costs associated with the education of front-line lenders and brokers, including system updates:

- Total of 1937 branches of major lenders
    - 16 hours of additional training across 8 employees per branch
- Total of 480 branches of other lenders
    - 6 hours of additional training across three employees per branch
- Total of 16,968 mortgage brokers (Mortgage & Finance Association of Australia)
- Total of 27 approved lenders participating in the schemes
- 10 additional hours for each lender to update systems
- Using the Office of Best Practice Regulation estimate for business costs at $73.05 per hour

Estimated average regulatory costs associated with the education of front-line lenders and brokers, including systems updates, is $0.981 million per year.

The following additional assumptions were made to estimate the regulatory costs associated with ongoing administrative costs to lenders through processing additional loans:

- Additional two hours for a lender to process a guarantee loan
- Additional hour for a lender to conduct reporting of new loans under new guarantees over 12 months (1 hour per month over 12 months, in accordance with NHFIC's monthly reporting requirements)

Estimated average regulatory costs associated with ongoing administrative costs to lenders through processing additional loans is $3.713 million per year.

The following additional assumptions were made to estimate the regulatory costs associated with processing defaults on additional loans:

- Default claim rate of 2 per cent (based on actuarial modelling of the scheme)
- Additional 5 hours for a lender to process default

Estimated average regulatory costs associated with processing defaults on additional loans is $0.184 million per year.

The total estimated average regulatory costs to lenders and brokers is $4.878 million per year.

Average annual regulatory costs (from business as usual)				
Change in costs ($ million)	Business	Community organisations	Individuals	Total change in cost
Total, by sector	$4.88	$0	$0.81	$5.69

Option 3

This option would support a smaller cohort of Australians into home ownership than Option 2. It would provide broadly the same degree of support currently provided under existing schemes, albeit on an ongoing basis (the New Home Guarantee is currently scheduled to expire at the end of the current financial year). As such, Option 3 would not represent a significant increase in the degree of support for home ownership than is currently in place.

The associated risks of this option and impacts on the LMI sector and the housing market are commensurately lower than for Option 2. Specifically:

- A scheme of 30,000 places each year would be equivalent to around 17 per cent of the private LMI market (by number of loans). This is a much smaller impact on the LMI market than Option 2 and would be associated with a lower risk of a significantly adverse impact on the ongoing viability of the market. This further reduces the risk of any possible flow on effects from a smaller LMI market such as higher insurance premiums.
- As previously discussed, the impact of the scheme on house prices is difficult to disaggregate from other influences on the market, however considering the fundamental theory that an increase in demand will increase prices, all other factors being held constant, Option 3 presents a lower potential increase in price noting that regardless of which option is chosen the effect of the guarantee scheme on prices is likely to be small.
- Similar to Option 2, given the existing financial experience with the current FHLDS scheme and lenders' responsible lending obligations, the risk of default and therefore the realisation of the Government's liabilities under the guarantee scheme is modest.

Methodology used to estimate regulatory costs to individuals – Option 3

All assumptions and methodologies remain the same as under Option 2, with the only difference being the smaller number of guarantee places available each year as outlined in section 3 above.

The total estimated average regulatory costs to individuals under Option 3 is $0.392 million per year.

Methodology used to estimate regulatory costs to lenders and brokers- Option 3

All assumptions and methodologies remain the same as under Option 2, with the exception of the additional assumptions listed above.

Estimated average regulatory costs to educate front-line lenders and brokers, including systems updates, is $0.981 million per year.

Estimated average regulatory costs associated with ongoing administrative costs to lenders through processing additional loans is $1.813 million per year.

Estimated average regulatory costs associated with processing defaults on additional loans is $0.089 million per year.

The total estimated average regulatory costs to lenders and brokers is $2.884 million per year.

Average annual regulatory costs (from business as usual)				
Change in costs ($ million)	Business	Community organisations	Individuals	Total change in cost
Total, by sector	$2.88	$0	$0.39	$3.28

5. Who did you consult and how did you incorporate their feedback?

Various consultations have taken place since the start of the FHLDS program to understand the viewpoints of the main stakeholders affected by the program.

The consultation process undertaken as part of the recently completed NHFIC Review comprehensively assessed the impacts of the FHLDS. The Review itself and the feedback provided to the Review by LMI providers and lenders provides a suitable foundation for an assessment of stakeholder views on government guarantee schemes.

Some LMI providers found that the FHLDS appears to allow borrowers to purchase a property approximately one to two years earlier than they otherwise would have. Their analysis found that likely in excess of 75 per cent of FHLDS participants would have been eligible to borrow for a property without the support of the scheme within 12 to 30 months of

their FHLDS-assisted purchase. This suggests that the majority of beneficiaries of the FHLDS are ‘accelerated buyers’ – those who would have been able to purchase a property, either with the support of LMI or with a full 20 per cent deposit, one to two years later, and is consistent with the widespread view heard by the Review. This feedback suggests that the scheme is operating as intended however concerns were raised that the scheme could have an impact on the LMI sector. Analysis undertaken in sections 2 and 4 has shown that although the existing scheme and its proposed expansion is likely to reduce the demand for LMI products, the size of the scheme’s expansion is unlikely to substantially affect the viability of the LMI sector.

One LMI provider has suggested that consideration be given to supporting an alternative proposal whereby LMI premiums are tax deductible for first home buyers. This would result in a smaller benefit to eligible home buyers than a government guarantee as the value of the tax deduction is limited to the marginal tax rate of the purchaser. The impact of this on the LMI sector would likely be positive, as the proposal would lower the cost of LMI for all eligible borrowers and could increase demand for LMI from prospective borrowers who would otherwise fund their purchase without the need for LMI (for example, through a family guarantee or larger savings). However, many of the benefits will likely flow to those on higher marginal tax rates, compared to low- and middle-income earners who have been identified as needing the most assistance in section 1. Although a tax deduction is a smaller benefit to the individual than a guarantee, the proposal implies that a larger cohort would be able to access the scheme as no limits are proposed to the number of applicants. Such an uncapped scheme would increase the financial risk to Government. Therefore, this proposal is considered to be less effective at supporting home buyers to enter the market sooner than that of a government guarantee scheme.

Further, additional funding would be required for the Australian Taxation Office to establish and administer such a program. It is anticipated the administration costs to establish the appropriate systems and reporting infrastructure would be high, given there are currently no capabilities to capture this information under existing systems. Additional costs would also be required to establish appropriate measures to minimise integrity risks to the program, noting that some integrity risk is likely to remain with such a program. The Review found that more and better data is needed to fully evaluate the behavioural impacts of the FHLDS. While initial data positively points towards the effectiveness of the program, the FHLDS scheme rules were recently expanded to include behavioural questions for first home buyers to answer as part of a questionnaire. Furthermore, the Review recommended that there would be merit in considering whether expanded Government home deposit guarantees could be more precisely targeted to those that most need the assistance. The Home Guarantee Scheme seeks to provide targeted support for cohorts in most need including regional home buyers, older Australians and single parents with dependants.

Banks have provided favourable feedback on the FHLDS and are supportive of the scheme and its recent expansions. The Commonwealth Bank of Australia has outlined that the FHLDS and its subsequent expansion has been effective in helping increase purchasing activity amongst first home buyers across the country. This has resulted in positive flow on effects into other parts of the economy such as the construction industry. The National Bank of Australia has also reflected similar positive feedback regarding the Scheme.

Furthermore, the *National Housing Finance and Investment Corporation Act 2018* requires that a review of NHFIC's activities to assist home buyers to enter the market is undertaken every 12 months. These reviews would consider stakeholder's views and would inform decision making around the Scheme.

6. What is the best option from those you have considered?

Given the difficulties that many Australians face in securing a deposit in a market with increasing house prices and low interest rates, a key objective with a proposed policy is to ensure that Australians are able to comfortably settle in their homes sooner or less expensively than would otherwise be possible in the absence of Government support.

Given the uptake of FHLDS places in previous years and the positive reviews from some stakeholders, the expansion of the FHLDS is an appropriate way of encouraging home ownership. This effectively rectifies the ever-increasing deposit hurdle faced by many prospective home buyers, in an environment where house prices have increasingly become unaffordable for many.

Further, given the recommendation in the NHFIC review of targeting places in times when the guarantee schemes are further expanded, specific objectives are targeted with the Regional Home Guarantee, Mature Home Guarantee and the New Home Guarantee.

The need for Australians to invest in their own home is important, especially with all the associated benefits of home ownership. An increase in places will be required to ensure this goal is achieved and is why Option 2 is preferred.

A key indicator of whether the Scheme has achieved its objectives will be whether the Scheme is able to operate alongside a viable and profitable LMI industry that continues to support other first home buyers access to the market. Maintaining the viability of the LMI industry is imperative, as it allows potential home buyers that don't qualify for the Scheme to enter the property market sooner than they would otherwise would.

The decision on whether to adopt this policy is to be made by Government and will be informed by this Regulation Impact Statement two-pass process.

7. How will you implement and evaluate your chosen option?

Implementation

Given that the Scheme is an expansion of an existing program, implementation challenges should be minimal as Treasury and the delivering agency, NHFIC, have the necessary experience to effectively manage the roll out of new guarantees.

One implementation consideration is ensuring that the price caps do not become a limitation for access to the Scheme.

Guarantees under the Scheme will align with the price caps offered under the FHLDS or NHG, as outlined below.

Region	FHLDS & Family Home Guarantee Price Cap	New Home Guarantee Price Cap
NSW - capital city, regional centres (Newcastle, Lake Macquarie & Illawarra)	$800,000	$950,000
NSW – other	$600,000	$600,000
VIC – capital city, regional centre (Geelong)	$700,000	$850,000
VIC – other	$500,000	$550,000
QLD – capital city, regional centres (Gold Coast & Sunshine Coast)	$600,000	$650,000
QLD – other	$450,000	$500,000
WA – capital city	$500,000	$550,000
WA – other	$400,000	$400,000
SA – capital city	$500,000	$550,000
SA – other	$350,000	$400,000
TAS – capital city	$500,000	$550,000
TAS – other	$400,000	$400,000
ACT	$500,000	$600,000
Northern Territory	$500,000	$550,000
Jervis Bay Territory & Norfolk Island	$550,000	$600,000
Christmas Island & Cocos (Keeling) Island	$400,000	$400,000

Property price caps have been set so that only modest properties in regional towns and capital cities can be purchased. Recent data on purchases under the Scheme indicates that most applicants are purchasing a property that is comfortably under the price cap, often around 75-90 per cent relative to the price cap. Regular monitoring of the purchase price to price cap ratio will ensure that the cap remain fit for purpose.

It is anticipated that the current loan and guarantee application process will continue, and the guarantees will be offered by the participating panel of lenders. Lenders' processes may need to be upscaled to account for the extra places, however, this would not be expected to be intensive.

While the intention is to have the proposed Scheme commence as soon as possible, timing of necessary legislative amendments, and therefore the commencement date of the Scheme, is subject to the Government's legislative agenda.

Evaluation

NHFIC releases a comprehensive annual review of the existing FHLDS program (and associated extensions) which details the performance of the program, providing data on the applicants utilising the guarantees and the properties purchased under the scheme. This data provides a valuable information base through which a detailed analysis of the program can be undertaken.

Furthermore, as previously mentioned, the *National Housing Finance and Investment Corporation Act 2018* requires that a review of NHFIC's activities to assist home buyers to enter the market is undertaken every 12 months. These reviews are a useful formal tool to evaluate the effectiveness of the Scheme and would be used to inform further decision making on the Scheme and its operation.