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Regulation Impact Statement

Regional First Home Buyer Guarantee

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Regulation Impact Statement

Background

This document is an addendum to the 'Home Guarantee Scheme' regulation impact statement (RIS) (22-01418).

This addendum provides analysis of the incremental regulatory impacts associated with the 'Regional First Home Buyer Guarantee' (previously announced as the Regional First Home Buyer Support Scheme). The previous Government's Regional Home Guarantee was agreed in the 2022-23 Budget but had not yet been enacted at the calling of the 2022 Federal Election. The Regional First Home Buyer Guarantee is an election commitment of the Labor Government.

The 'Home Guarantee Scheme' RIS was assessed by the Office of Best Practice Regulation (OPBR) in March 2022 and provides analysis of the regulatory impacts associated with a similar Regional Home Guarantee. Both the Regional Home Guarantee and the Regional First Home Buyer Guarantee seek to assist regional homebuyers to purchase a home sooner and with a smaller deposit. However, there are minor policy differences between the schemes, namely non-first homebuyer eligibility and property type eligibility. Drawing on the existing analysis in the 'Home Guarantee Scheme' RIS, and in meeting the OBPR's regulatory impact analysis requirements, this addendum will consider the regulatory impacts associated with these differentials only.

Regional Home Guarantee.

The proposed Regional Home Guarantee was limited to new homes in eligible regional areas only, and included both existing regional first home buyers and first home buyers not currently living in regional areas. Eligibility would have allowed some buyers who have previously owned property but hadn't done so for at least three years.

Name	Cohort	Income & price caps	Property type	Minimum deposit	Number of Guarantees per FY1
Regional Home Guarantee	FHBs and some non-FHBs. No restrictions on current address.	Consistent with HGS	New homes in regional areas, including regional centres	5 per cent	10,000, to 2024-25.

By offering guarantees to applicants not living in regional areas, including those who may not be first home buyers, the Regional Home Guarantee would likely have had the effect of encouraging the movement of city residents to regional areas. In addition, limiting guarantees to new homes only would likely have the effect of increasing demand for new construction relative to demand for existing dwellings.

While some first home buyers in regional areas may have benefited from the Regional Home Guarantee, previously scheduled to commence on 1 October 2022, it was not a program primarily targeted at first home buyers. Rather, it was a program open to all buyer types that was designed to facilitate additional dwelling construction in regional areas. As a result, regional first homebuyers would have needed to compete with other buyers for support under the scheme and would have been limited to purchases of new homes only.

Had it been implemented, the Regional Home Guarantee would have had the effect of driving substantial additional demand for new dwelling construction in regional areas during a period when the regional construction sector is already facing substantial cost pressures and capacity constraints. Treasury stakeholder consultation and analysis of Australian Bureau of Statistics (ABS) data suggest that building material costs are rising significantly and the pipeline of work for housing construction is at record levels. There were around 103,000 detached houses under construction as at March 2022 - a new record. This compares to a typical number of around 60,000 prior to the pandemic.2 Owing to capacity constraints amid a record pipeline of work, house construction input prices have risen by 17.3 per cent through the year to the June quarter 2022.3

The Regional Home Guarantee would also have further encouraged the flow of population from the capital cities to the regions, again putting additional pressure on regional infrastructure and prices.

The Office of Best Practice Regulation's (OBPR's) assessment (OBPR22-02423) was that the quality of the analysis in the RIS was adequate to inform a decision.

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

Housing markets in regional Australia have become increasingly unaffordable for first home buyers in recent years. A combination of low interest rates and strong population growth have resulted in rapid growth in prices for existing dwellings, while high demand, labour shortages and supply chain constraints have put pressure on the construction sector.

Over the past year, there has been an increase in net internal migration to the regions, which has placed upward pressure on house prices. The net flow of capital city residents moving to the regions is at historic levels, with 49,000 city dwellers moving to the regions in the year to June 2021, more than three times the pre-pandemic level of 15,000 in 2019.[4] As people shift to remote working, there is an expectation of higher future population growth in the regions.

House prices have risen substantially over the past year, from already high levels, and regional areas have experienced particularly significant growth. Over the year to June 2022, regional housing prices grew by 19.9 per cent, compared to 8.7 per cent in combined capital cities.[5]

The impact of recent increases in house prices in regional Australia is not felt equally by all households. Affordability has not significantly worsened for homebuyers who already own property as these households have benefitted from recent increases in dwelling prices and can draw on this existing equity when looking to move or upgrade. These households have also benefited from the historically low interest rates in recent years.

First home buyers, however, face increasing difficulties entering the housing market – particularly those that are priced out of capital city markets and those on low incomes already living in the regions. Not only are high house prices necessitating higher average loan amounts, the time taken for prospective first home buyers to save a typical deposit has also increased. Further compounding this problem is an increase in rents in regional areas which reduces the disposable income households have available for saving for a deposit. National advertised rents have risen by 17.2 per cent since March 2020, with advertised rents in regions (up 24.3 per cent) outpaced capitals (up 14.8 per cent).[6] First home buyers in regional Australia face a high and rising deposit hurdle – requiring on average 10.5 years to save for a deposit.[7]

For regional Australians wishing to purchase in the near term but who 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 homeownership 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.

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.[8] Where an upfront LMI premium is charged, borrowers typically capitalise the

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1 Unused guarantees from each financial year may be eligible for roll over into the subsequent financial year.
2 ABS, Building Activity
3 ABS, Producer Price Index
4 Treasury, Centre for Population estimates
5 Treasury, based on CoreLogic data
6 Treasury, based on CoreLogic data
7 Treasury calculation, based on CoreLogic data
8 Based on a 30-year mortgage term for an owner occupier, excluding stamp duty (https://www.genworth.com.au/products/tools/lmi-fee-estimator).

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[9].

For prospective homebuyers 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).

Support through the First Home Guarantee program will address the deposit hurdle problem faced by many first home buyers in regional Australia. However, despite a recent increase in available places to 35,000 per year, the speed with which each year's available allocation of First Home Loan Deposit Scheme places has been exhausted suggests there is a large unmet demand for places.[10] As a consequence, it is likely that the First Home Guarantee will be over-subscribed, and many eligible first home buyers in regional areas are likely to miss out on support.

Increasing the number of places available under the First Home Guarantee would lower the likelihood of first homebuyers in regional areas missing out on support. However, this scheme is available to both city and regional first home buyers, which means ensuring access for eligible first homebuyers in regional areas would require a much larger increase in the total number of available places than required for regional applicants alone.

2. Why is Government action needed?

As outlined above, regional housing markets are becoming less affordable, particularly for first homebuyers on low incomes. While LMI offers a private market solution to prospective first homebuyers with relatively small deposits, it can add significantly to the cost of borrowing, delay access to homeownership for some, and is not accessible to all potential homebuyers.

The Commonwealth Government, through its operation of the First Home Loan Deposit Scheme (FHLDS), the New Home Guarantee, and the Family Home Guarantee, has demonstrated it has the capacity to intervene successfully to support homeownership for those who are able to secure one of the limited number of guarantee places made available under these programs. For more information on the schemes' performance and strong demand, see the 'Home Guarantee Scheme' RIS.

Despite the high level of demand across all the programs, key lending indicators show that guarantee backed loans are performing well. As at 31 May 2022, 43,704 guarantees had been issued. Of these, no scheme-backed loans had defaulted, though this pre-dates the recent interest rate increases.[11] 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 from a median of 24.5 per cent in 2020-21 to 23 per cent in 2021-22.[14]

9 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.

10 For further detail on demand for the First Home Loan Deposit Scheme, see the Report of the Statutory Review of the Operation of the *National Housing Finance and Investment Corporation Act 2018*

11 First Home Loan Deposit Scheme and New Home Guarantee Trends & Insights Report 2020–21

3. What policy options are you considering?

Implementing the Regional First Home Buyer Guarantee is an election commitment of the Government. As such, the two options considered: are maintaining the status quo by continuing to operate the existing Home Guarantee Scheme (**Option 1**); or implementing the Regional First Home Buyer Guarantee (**Option 2**).

The RIS considered for the expansion of the Home Guarantee Scheme, including the proposed Regional Home Guarantee, provided the foundation for this Addendum RIS. The Addendum RIS puts forward the option of the proposed Regional First Home Buyer Guarantee, which involves somewhat different parameters from the previously proposed Regional Home Guarantee.

The main differences between the Regional Home Guarantee and Regional First Home Buyer Guarantee is that the Regional First Home Buyer Guarantee will: require a local residency test, limit eligibility to First Home Buyers only, and allow both new and existing property types.

Regulatory costs to individuals, lenders and brokers are expected to be almost identical between the Regional Home Guarantee and Regional First Home Buyer Guarantee. The original proposal in the Home Guarantee Scheme Regulation Impact Statement, included aggregated costs across the whole three part proposal. And as the regulatory costs of the Regional Home Guarantee and Regional First Home Buyer Guarantee is expected to be almost identical, regulatory costs are not further considered in this Addendum Regulatory Impact Statement.

For more information on regulatory costs please see the Home Guarantee Scheme Regulation Impact Statement.

Option 1: The status quo

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

Name	Cohort	Income & price caps	Property type	Minimum deposit	Number of Guarantees per FY12
First Home Guarantee	First home buyers	Income caps: $125k/$200k Price caps: existing	New & established	5 per cent	10,000 per annum, ongoing
Family Home Guarantee	Single parents	Income cap: $125k Price caps: existing	New & established	2 per cent	10,000 over four years from 2021-22

While these schemes assist homebuyers on moderate to higher incomes (income caps of $125,000 for singles and $200,000 for couples apply) to overcome the deposit hurdle, they do not address the serviceability hurdle – applicants still need to have sufficient means to service a high loan-to-valuation ratio loan.

12 Unused guarantees from each financial year may be eligible for roll over into the subsequent financial year.

Option 2: The Regional First Home Buyer Guarantee.

Under Option 2, the Regional First Home Buyer Guarantee would be implemented in place of the Regional Home Guarantee.

Name	Cohort	Income & price caps	Property type	Minimum deposit	Number of Guarantees per FY[13]
Regional First Home Buyer Guarantee	FHBs that have been living in regional Australia for at least 12 months.	Consistent with HGS	New *and* existing homes in regional areas	5 per cent	10,000, to 2024-25
Regional Home Guarantee	FHBs and some non-FHBs. No restrictions on current address.	Consistent with HGS	New homes in regional areas, including regional centres	5 per cent	10,000, to 2024-25.

The Regional First Home Buyer Guarantee (RFHBSS) builds upon the Commonwealth Government's existing Home Guarantee Scheme programs to support earlier access to homeownership for first home buyers in regional Australia.

Guarantees under the Regional First Home Buyer Guarantee would be able to be used to purchase both new and existing dwellings in regional areas but would only be available to first home buyers who can demonstrate they have lived in a regional area for at least the past 12 months.

The proposed eligibility criteria effectively make the Regional First Home Buyer Guarantee an extension of the larger First Home Guarantee scheme. Given the First Home Guarantee is expected to be oversubscribed, this would have the effect of ensuring that first home buyers in regional areas have access to an additional reserve of guaranteed places, should places under the First Home Guarantee be exhausted.

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

Option 1 Status Quo

Under the status quo, the existing guarantee schemes would support some households into homeownership. This would continue to represent a relatively small share of annual first home buyer activity and a small share of overall mortgage lending. There are no additional regulatory costs or savings associated with this option.

As above, regional housing markets are becoming less affordable and LMI can add significantly to the cost of purchasing a home. Without additional government support, first homebuyers in regional Australia who miss out on accessing the First Home Guarantee will have to wait longer to enter the market or will have to pay more with LMI.

13 Unused guarantees from each financial year may be eligible for roll over into the subsequent financial year.

Option 2 Regional First Home Buyer Guarantee

Option 2 implements the parameters of the Regional First Home Buyer Guarantee. This would result in the 10,000 funded places being made available exclusively to first home buyers who are existing regional residents and expanding property eligibility to include existing homes. All other parameters are consistent with Option 1.

The objectives of this policy include:

- Supporting prospective homebuyers in regional areas into homeownership; and
- Targeting support to only those that are residents of the region in which they are intending to purchase.

Effect of confining eligibility to first home buyers

Dwelling prices have increased significantly in regional areas in recent years, posing a significant barrier for first home buyers to access the market.[14] By limiting access to home guarantees under this program to first home buyers, this option ensures that support is effectively targeted to the cohort most in need of assistance.

Effect of confining eligibility to buyers who have lived in regional areas for at least 12 months

The 12-month residency requirement ensures that support under the program will not have the unintended consequence of encouraging a further increase in population flows between capital cities to regions already facing infrastructure constraints and rapid price rises due to increased demand. It also ensures that support remains targeted to the cohort most in need of assistance.

The requirement to provide evidence of 12-months residency is unlikely to impose a material additional regulatory burden on the applicant or lender, as similar information already needs to be provided by borrowers when applying for finance.

Effect of expanding eligibility to include existing homes

Expanding eligibility to include existing homes will have the effect of reducing demand for new dwellings and increasing demand for existing dwellings relative to Option 1.

Long-term housing affordability relies on the provision of new supply. As such, measures that encourage new dwelling supply will generally deliver a net benefit for homebuyers in the long term. However, capacity constraints and labour shortages in the construction sector (see discussion in Section 2) mean that any measure that increases demand for new dwellings in the current environment may not meaningfully increase overall supply. Rather, bringing forward demand for new dwellings when construction capacity is fully utilised may only result in price increases for all buyers.

Measures that increase demand for existing housing will result in some increase in prices for established dwellings. As a result, expanding eligibility to established dwellings may have a small effect on established dwelling prices. However, as the number of available places is small relative to the overall stock of established dwellings, the size of this impact is likely to be extremely small. Moreover, by splitting demand between existing and new dwellings, the impacts of the scheme on demand and prices will be spread across existing and new dwellings, further mitigating the potential impact on aggregate dwelling prices.

14 Over the year to June 2022, regional housing prices grew by 19.9 per cent (Treasury, based on CoreLogic data).

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

Given the minor policy differences considered in this regulatory analysis, being first home buyer and property type eligibility, the scope of consultation in preparing this addendum has been limited.

However, consultation has taken place with the National Housing Finance and Investment Corporation (NHFIC) on the design and implementation of the Regional First Home Buyer Guarantee and this feedback has been incorporated in this analysis to the extent it relates to first home buyer and property type eligibility.

Additionally, the consultation process undertaken as part of the recently completed NHFIC Review comprehensively assessed the impacts of the FHLDS and NHFIC's activities to support first home buyers. 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.

For more information on consultation relating to LMI, please see 'Home Guarantee Scheme' RIS.

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

Given the difficulties that many households in regional Australia face in securing a deposit in a market with high house prices and rising interest rates, a key objective of the policy is to ensure that regional Australians are able to buy their own home sooner than would otherwise be possible in the absence of Government support. This is consistent with the Government's objective of supporting those in regional Australia into homeownership.

Given the high demand for Home Guarantee Scheme places in previous years, the annual allocation of First Home Guarantee places is likely to be exhausted each year. As such, confining scheme eligibility to regional first home buyers is an appropriate way of encouraging homeownership amongst those living in regional Australia facing significant difficulty entering the market. This will assist in overcoming the deposit hurdle faced by many prospective regional first home buyers, in an environment where house prices have increasingly become unaffordable for many.

Due to the current supply chain constraints in the construction sector, and particularly in the regional construction sector, expanding property type eligibility to include existing dwellings will ensure demand is more evenly distributed in the housing market and avoid exacerbating current pressures.

For these reasons, compared to the status quo, the preferred option is Option 2, implementing the Regional First Home Buyer Guarantee (as distinct from the previous Government's proposal to introduce the Regional Home Guarantee).

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

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

Implementation

Given that the Regional First Home Buyer Guarantee will operate alongside the existing low deposit guarantee schemes, implementation challenges should be minimal as the administering agency, NHFIC, and the existing panel of participating commercial lenders have the necessary experience to effectively manage the roll out of the new scheme.[15]

The current loan and guarantee application process will continue, and the guarantees will be offered by the participating panel of lenders.

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 homebuyers that don't qualify for the Scheme to enter the property market sooner than they would otherwise would.

It is anticipated the Regional First Home Buyer Guarantee will commence late-2022, subject to necessary amendments to the *National Housing Finance and Investment Corporation Investment Mandate Direction 2018*.

Evaluation

Building on data collection and analysis practices for the existing Home Guarantee Schemes, observed outcomes for the Regional First Home Buyer Guarantee will be evaluated against, but not be limited to, the following:

- Supporting up to 10,000 regional first homebuyer purchases each year;
- Feedback gathered from participants indicating that they would not have been able to enter the market, or enter at a much later date, in the absence of the scheme;
- The scheme's impact on different target cohorts, including key workers and mature women;
- The scheme is able to operate alongside a viable private market for LMI; and
- The credit performance of loans written under the scheme evolves in line with comparable non-scheme-backed loans.

NHFIC releases a comprehensive annual review of the existing FHLDS program (and associated extensions), provided in the annual Trends and Insights Report 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 can be undertaken for program evaluation and design, as well as informing other program and policy purposes. This includes analysis of the impact of the schemes on different target cohorts, such as single parents, mature women and long-term renters. It is anticipated the Regional First Home Buyer Guarantee will be included in this annual review.

Further, section 57A of the *National Housing Finance and Investment Corporation Act 2018* requires that the Minister must cause a review of NHFIC's activities to assist homebuyers 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.

15 Note, price caps which apply to the FHLDS (and will apply to the Regional First Home Buyer Support Scheme), will update from 1 July 2022.