

4 November 2019

The Manager  
Social Policy Division  
Treasury  
Langton Crescent  
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By email: [housingconsultation@treasury.gov.au](mailto:housingconsultation@treasury.gov.au)

Dear Sir/Madam

### **National Housing Finance and Investment Corporation Investment Mandate**

The Insurance Council of Australia<sup>1</sup> (Insurance Council) appreciates the opportunity to comment on the *National Housing Finance and Investment Corporation Investment Mandate Amendment (First Home Loan Deposit Scheme) Direction 2019* (the Investment Mandate).

The Insurance Council and its members strongly support the objective of assisting first home buyers with low deposits to obtain a home loan and buy their first home. Lenders' Mortgage Insurance (LMI) has helped borrowers purchase properties with deposits of as low as 5% since 1965, when it was initially introduced by the Government for the purpose of providing access to home ownership for a broader segment of the population.

As such, we support the central objective of the Government's First Home Loan Deposit Scheme (the Scheme), namely to facilitate earlier access to home ownership for certain first home buyers provided the Government Scheme does not operate in a way that "crowds out" or impacts on the viability and/or ability to achieve adequate returns to support capital invested in the private LMI market<sup>2</sup>. As the *Explanatory Memorandum to the National Housing Finance and Investment Corporation Amendment Act 2019* (the Act) notes:

The development of the Scheme has prioritised the maintenance of a viable and profitable LMI industry, as LMI enables high-LVR lending and benefits the financial system more broadly. LMI allows potential home buyers the ability to enter the property market sooner than they would otherwise be able to. Without LMI, potential

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<sup>1</sup> The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent approximately 95 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. June 2019 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of \$48.4 billion per annum and has total assets of \$128.4 billion. The industry employs approximately 60,000 people and on average pays out about \$151.4 million in claims each working day.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as lenders' mortgage insurance, product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

<sup>2</sup> Paragraphs 2.12 and 2.14 of the *Explanatory Memorandum to the National Housing Finance and Investment Corporation Amendment Bill 2019*.

home buyers with deposits of less than 20 per cent would not ordinarily be able to obtain a mortgage. In addition to insuring lenders against the higher risks involved in lending to FHBs, LMI providers also provide a ‘second pair of eyes’ on the loan assessment process. Taken together, this increases the willingness of lenders to lend to FHBs. (paragraph 2.32).<sup>3</sup>

While the objective of the Scheme is clear, we are concerned that the eligibility criteria set out in the Investment Mandate fails to achieve the Government’s stated objective. In particular, section 29C (2)(g) of the Investment Mandate limits the application of the Scheme to residential properties of a value not in excess of the price caps set out in section 29F.

Based on analysis by the Insurance Council’s members, 50 to 65 per cent of first home buyers that utilise LMI to purchase their first home fall within the prescribed price caps. As such, the price caps fail to mitigate the risk that the Scheme crowds out the private LMI market. The Insurance Council submits that the eligibility criteria could better target first home buyers who are currently unable to enter the housing market.

As discussed in the Explanatory Memorandum to the Act and in second reading speeches<sup>4</sup>, a key design feature of the Scheme is that it will be limited to 10,000 guarantees a year. This is implemented through s29I (1) of the Investment Mandate which provides that “The NHFIC must not issue more than 10,000 guarantees in a financial year”.

Given the high degree of community interest that has been generated in the Scheme, there is potential for the majority of the overall number of guarantees to be provided in the early months of the Scheme’s operation. In order to moderate the possible disruption to the LMI industry, the Insurance Council suggests that for the period 1 January 2020 to 30 June 2020, the number of guarantees should be limited to 5,000.

Separately, the Insurance Council notes that section 57A of the Act requires a review of the Scheme every twelve months to ensure that its objectives are being met. The Insurance Council and its members are willing to share data and analysis to support that review.

If you have any questions or comments in relation to our feedback, please contact John Anning, the Insurance Council’s General Manager Policy, Regulation Directorate, on (02) 9253 5121 or [janning@insurancecouncil.com.au](mailto:janning@insurancecouncil.com.au).

Yours sincerely



Robert Whelan  
Executive Director and CEO

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<sup>3</sup> The role and benefits of LMI are detailed in Appendix A

<sup>4</sup> See p6, Second Reading Speech by the Hon Michael Sukkar MP (dated 12 September 2019)

## **VALUE AND BENEFIT OF LENDERS' MORTGAGE INSURANCE**

LMI plays a key role in facilitating affordable and accessible home ownership in Australia and broadly supporting and facilitating competition between lenders in Australia's home lending market.

### *LMI helps improve access to home ownership*

By enabling those who would otherwise have difficulty obtaining a home loan due to lack of a 20 per cent deposit or an established credit repayment history, LMI is particularly beneficial for first home buyers. With the benefit of LMI, many first home buyers are able to:

- buy, move into and accumulate equity in their home much sooner; and
- obtain a home loan that may otherwise not be available if the lender could not manage the risk or capital requirements.

LMI is a mechanism which enables a lender to offset additional risks associated with higher risk loans, such as loans to first home buyers.

### *LMI supports the financial system and continuation of lending through economic cycles*

LMI provides risk transfer and diversification to lenders with most cover relating to high Loan to Value Ratio (LVR) lending. LMI providers are prudentially regulated. Their capital requirements are set to withstand 1 in 200 year stress events. LMI providers typically diversify their risk offshore through the use of reinsurance, providing foreign capital to support an Australian based downturn. The combination of capital and reinsurance promotes stability across the wider financial system. Furthermore, the use of international reinsurance provides access to cost effective risk mitigation, which reduces costs to insurers and ultimately reduces costs to borrowers.

LMI is designed and priced for a long term through-the-cycle view and contributes to absorbing the effects of economic cyclical downturns (such as in the aftermath of the global financial crisis). It facilitates the continuation of home lending at the bottom of a cycle and helps to maintain prudent lending at the top of a cycle.

In addition to increasing accessibility and affordability of housing, LMI plays a much broader role in the financial system by ensuring responsible residential lending standards are maintained by providing oversight of, and audit services to lenders.

### *LMI supports competition in the Australian residential mortgage lending market*

LMI helps many lenders operating in the Australian mortgage market compete for business.

The availability of LMI assists smaller lenders to compete with larger lenders (i.e. the major banks) which would otherwise enjoy a competitive advantage in the high LVR segment due to their balance sheet capacity to accommodate its higher risk and their enjoyment of the benefits of economies of scale and regulatory capital. This is particularly important for lenders with geographic concentration, where LMI plays a critical role in their market

participation, enabling them to offer home loans in, for example, regional and rural Australia or other states and territories.

Non-authorized deposit taking institutions (non-ADIs) (lenders that are not regulated by APRA) also use LMI when offering high LVR mortgages in Australia.

LMI provides credit enhancement that underpins the mortgage-backed securitisation market, enabling both ADI and non-ADI lenders to access funding at competitive rates. Securitisation promotes competition in the home lending market, enabling non-ADI lenders and ADIs to compete with larger lenders on pricing and other features.