

24 September 2019

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

By email: economics.sen@aph.gov.au

Dear Mr Gaczol

National Housing Finance and Investment Corporation Amendment Bill 2019

The Insurance Council of Australia¹ (Insurance Council) would like to thank the Committee for the opportunity to comment on the *National Housing Finance and Investment Corporation Amendment Bill 2019* (the Bill).

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 profitability of the private LMI market².

¹ 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).

² Paragraphs 2.12 and 2.14 of the *Explanatory Memorandum* to the Bill.

Viability of the private Lenders' Mortgage Insurance market

In this respect, we welcome the recognition in the *Explanatory Memorandum* to the Bill (the *Explanatory Memorandum*) of the importance of a private LMI market. The *Explanatory Memorandum* notes that:

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 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).

As discussed in the *Explanatory Memorandum* and the second reading of the Bill, three features aim to ensure that the Scheme will complement rather than compete with LMI. First, the Scheme will be limited to 10,000 guarantees a year, and property price caps will be set. Second, the guarantee will be removed if the outstanding loan balance falls below 80 per cent of the property purchase price.³ Third, there will be continued monitoring of the effect of the Scheme on the LMI market.⁴

We understand these features will be incorporated into the *National Housing Finance and Investment Corporation Investment Mandate Direction 2018*. However, the Insurance Council submits that these features are critical to the Scheme achieving its central objective and suggests the Bill be amended to embed these features in the operation of the Scheme. Without that, there is a possibility the subsequent governments could expand or alter the Scheme without recognising the potential implications for the private LMI sector.

Value and benefit of Lenders' Mortgage Insurance

The Insurance Council and its members welcome the recognition in the *Explanatory Memorandum* of the importance of a private LMI market. As the Committee appreciates, 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.

³ See p6, Second Reading Speech by the Hon Michael Sukkar MP (dated 12 September 2019)

⁴ See paragraph 2.35 *Explanatory Memorandum* to the Bill.

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 providing a “second set of eyes” assisting to ensure responsible residential lending standards are maintained by providing oversight of, and quality assurance 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-authorised 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.

Conclusion

The Insurance Council and its members are pleased that the Government has recognised the important role that the private LMI sector plays in the Australian housing market and the need to prioritise the maintenance of a viable and profitable LMI sector. As outlined above, we suggest to ensure the impact on the LMI sector is minimised, the Bill be amended to reflect the features described above. Once Parliament has passed the legislation, we look

forward to working with the National Housing Finance and Investment Corporation on implementation of the Scheme.

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.

Yours sincerely



Robert Whelan
Executive Director and CEO