RESERVE BANK
OF NEW ZEALAND
TE PŪTEA MATUA

SUMMARY OF SUBMISSIONS

Proposed removal of Loan-to-Value Restrictions

Summary of submissions – Removal of Loan-to-Value Ratio restrictions following the onset of COVID-19

1. A short, seven day, consultation period was completed by the Reserve Bank following the announcement on 21 April of the proposal to temporarily remove Loan-to-Value Ratio (LVR) restrictions. Banks and the general public were provided the opportunity to respond to the consultation. A short consultation period was necessary in order to respond in a prompt way following an unprecedented set of economic events. The Reserve Bank also directly approached a number of NGOs, including Māori and Pasifika groups to make them aware of the proposed changes, and to offer them a chance to provide feedback on the proposals.

2. Submitters from the public expressed a wide range of views, with over 70 submissions being received over the consultation period. The views of the public and other stakeholders are summarised below. These views were carefully considered by the Reserve Bank throughout the consultation period, and are responded to briefly at the end of this document, and some are more thoroughly considered in the Regulatory Impact Assessment (RIA).

Locally incorporated banks were in favour of the proposals

3. All locally incorporated banks who responded were in favour of removing LVR restrictions for one year, noting that this will allow banks to support customers through the impact of COVID-19.

Submitters from the public and other organisations in favour of the proposal noted the benefits to first home buyers and stabilising house prices

4. Many first home buyers were in favour of the proposal, noting that this would get them into the property market sooner. Some of them noted that their Kiwisaver balances had declined, and so they had lower deposit amounts with which to enter the market. Some submitters noted that it may make it easier for low income households to save a deposit, including for Māori and Pasifika households. A few submitters also noted that this will also allow investors to come back into the market, who may have been disincentivised due to other government policy, noting the need for more rental properties.

5. Those submitters in favour of the proposal noted that it would be beneficial for stabilising house prices, given a likely house price decline and some forced property sales for those having trouble meeting debt obligations in the future. Some submitters noted that banks' response to the removal of LVR requirements would be important, noting that banks should still adopt sensible deposit/equity requirements for investors and owner-occupiers.

Submitters against the proposal expressed a broad range of views

6. Of those submitters that were against the removal of the LVR policy, many were concerned about potential adverse impacts on financial stability, such as the risk of bank failure. They noted that the current economic circumstances are highly uncertain, and they expressed concern that removing restrictions would increase the level of household and personal indebtedness at a time when taking on new debt should be discouraged. These submitters noted that the removal of the policy could encourage banks to undertake significant new lending at high LVRs against potentially declining house prices, and that those who borrowed with no restrictions now would risk falling into negative equity. They also noted that the economy has

weakened and job security has reduced, and the ability of people to service a mortgage will likely decline in the coming months. Some submitters believed that this, in conjunction with the delay in implementing bank capital requirements, would lead banks to lend imprudently.

7. Many of the submitters arguing against the removal of LVR restrictions cited its success at achieving financial stability, as indicated by stress test results and 2019 review of the LVR policy. They noted that the policy has ensured banks are available to withstand a significant downturn, and questioned why the Reserve Bank would be considering removing LVRs given that they have been an effective tool for keeping the banking system secure. A couple of submitters noted that under the current LVR speed limit rules, most banks could still have enough room to lend to high LVR loans.

8. Submitters believed that the housing market is already overvalued, and the removal could continue to prop this up, with some believing that there is little evidence that there will be a significant decline in house prices. Related this point, submitters noted that further concentration of wealth in real estate would shift investment away from asset classes where it is needed, citing that it would beneficial for employment stability and the economy for capital to flow to business lending and equity markets instead of into property markets.

9. Some submitters also believed that the removal of the LVR policy would exacerbate existing housing affordability issues, and prop up housing inequality in New Zealand. These submitters noted that wealthy investors – with existing property portfolios as collateral and stable incomes – would be the ones who would benefit from the policy removal and low property prices, at the expense of first home buyers and over extended investors.

Submitters expressed a range of other ways of removing or relaxing LVR restrictions, with a particular focus on continuing to differentiate between owner-occupiers and investors

10. A number of submitters believed the removal of the LVR policy should only apply to owner-occupiers (including first home buyers) and that the investor LVR restrictions should continue to apply. Many cited that investors are the ones predominantly competing with the first home buyers. They noted that removal of the LVR policy, though allowing a greater number of potential buyers in the market, will simply push up the prices of entry-level properties for those that need housing. Some of these submitters noted that the current LVR policy is progressive, making competition for housing more even, as those with less property or equity currently do not have to compete on the same playing field as investors, arguing that this should continue.

11. Submitters also expressed alternative ways to remove or relax the LVR restrictions. Some suggested that the current policy should be re-calibrated to lower levels, often retaining a split between owner-occupiers and investors, and could be further lowered if necessary. Others suggested a shorter period of time for the removal should be adopted and reviewed regularly, or argued that the policy should be relaxed for owner-occupiers first, then investors. A couple of submitters suggested a more targeted approach be taken, suggesting a removal of LVR restrictions for existing mortgages, to ensure owner access to any needed bridge financing, but maintaining LVR restrictions for new and prospective purchases. A few submitters also suggested that LVR restrictions could be eased or removed primarily for new builds.

Submitters also raised other issues related to Government policy, including the introduction of a capital gains tax or a deposit guarantee scheme

12. A small number of submitters also believed that there was a need for a capital gains tax if the LVR policy is removed for investors, as this could encourage more non-productive debt on top of existing property market debt. They believed that without a capital gains regime the LVR restrictions have effectively been the only mechanism to slow the expansion of housing investment.

13. Some savers expressed concern around the absence of a deposit guarantee scheme and the impact that the LVR policy removal would have on bank lending, citing that this could increase the risk of bank failure and may increase the risk of loss of their savings. They argued that a deposit guarantee scheme should be introduced, especially if LVR restrictions were removed.

Response to submissions

14. The Regulatory Impact Assessment (RIA) considers a number of the possible risks raised in these submissions. In particular, in the current economic circumstances, banks are likely to tighten lending standards, rather than loosen them. LVR restrictions are unlikely to provide benefits to financial stability in these circumstances. Continuing with LVR restrictions at such a time could introduce some unintended consequences. These include risks that banks may be reluctant to provide mortgage deferrals, or may reduce funding available to the non-bank sector.

15. Given the current uncertainty around the economic outlook, the Reserve Bank considers it to be unlikely that banks will weaken lending standards to high risk borrowers. The more likely risk is that banks are overly cautious with lending to credit-worthy borrowers.

16. The Reserve Bank recognises that the impacts of an LVR restriction removal on first home buyers are uncertain. While the absence of LVR restrictions may reduce the size of the deposit required for a first home buyer, it may also increase the ability of investors to borrow to purchase housing. It is unclear exactly how these dynamics will play out in the future, particularly during a period where house prices are likely to be falling. As a result, the RIA concludes that the impact on first home buyers is ambiguous.

17. The Reserve Bank also recognises that removing LVR restrictions for only owner-occupied housing is another option. This option would clearly provide first home buyers an advantage relative to investors, as high LVRs would provide less regulatory impediment to first home buyers. However, this objective sits outside of the Reserve Bank's mandate and it is not clear that such an approach would increase financial stability relative to removing for both owner-occupiers and investors. Indeed, a situation where banks curtailed lending to investors due to concerns about LVR restrictions might add to financial instability.

18. Some points raised by submitters were not directly relevant to the LVR policy removal, such as those relating to a capital gains tax or deposit guarantee scheme, and so were unable to be considered by the Reserve Bank.

19. The Reserve Bank will closely monitor developments in the sector following the removal of LVR restrictions over the next 12 months. Ongoing supervisory and statistical reporting processes will support this.