Reserve Bank of New Zealand
Te Pūtea Matua

Framework for Debt-to-Income Restrictions – Regulatory Impact Assessment

3 April 2023

Non-Technical Summary

Debt-to-Income (DTI) restrictions – what are they?

DTI restrictions on residential mortgage lending set limits on the amount of debt borrowers can take on relative to their income. DTI restrictions complement other tools we use to support financial stability, including loan-to-value ratio (LVR) restrictions on residential mortgage lending.

What is the purpose of this document?

This document sets out our Regulatory Impact Assessment (RIA) for the introduction of a regulatory framework for DTI restrictions. This framework sets rules for the design and operation of DTI restrictions. We are publishing the final version of the regulatory framework alongside this RIA. The framework will enable banks to begin making the systems changes required to allow implementation of DTI restrictions in the future.

When will DTI restrictions be implemented?

We have not made a decision to activate DTI restrictions yet. Once banks' systems are ready, changes to Conditions of Registration would be needed to activate the restrictions. Banks have told us they need around 12 months to prepare their systems for possible implementation of DTI restrictions. Therefore, the earliest date we could do this is likely to be March 2024.

What are the main benefits and costs of DTI restrictions?

DTI restrictions support financial stability by limiting higher-risk mortgage lending, thus reducing the likelihood of a future housing-related financial crisis.

The costs of DTI restrictions include administrative costs for banks and allocative efficiency costs from reducing credit availability to some otherwise credit-worthy borrowers. Our analysis indicates that the potential benefits of DTI restrictions would significantly outweigh their costs. The DTI framework incorporates design elements that will mitigate efficiency costs – in particular, the use of exemptions for certain types of borrowers, and 'speed limits' which allow banks to continue extending some loans to borrowers above the DTI threshold. In addition, introducing DTI restrictions may enable us to loosen loan-to-value ratio (LVR) restrictions on residential mortgage lending while maintaining our financial stability objectives. This would have an offsetting benefit for allocative efficiency.

Since we are only proposing to put in place the regulatory framework for DTI restrictions at this stage, the costs that will be incurred are primarily administrative costs for banks, including changes to IT systems and training staff on the application of DTI restrictions. If activated, the costs and benefits of DTI restrictions will depend to a significant extent on how they are calibrated. We will assess the impacts of different calibrations separately prior to any decision to activate DTI restrictions. As part of this assessment we will also consider the interaction between DTI and LVR restrictions.

We acknowledge that the housing market is currently in a downturn and we do not see an immediate need to implement DTI restrictions. Therefore, an alternative option would be not to put in place the DTI framework now, but instead to wait and assess whether DTI restrictions are needed at a future stage of the housing cycle. While this would avoid administrative costs to banks in the short term, there is a significant chance that if the housing cycle turns and financial stability risks begin to rise, there would be insufficient time to put the framework in place to address these

risks. This is because banks have requested a lead time of 12 months to prepare their systems for the potential implementation of DTI restrictions.

How would DTI restrictions affect first-home buyers?

The impacts of DTI restrictions on first-home buyers will depend on how they are calibrated. However, our analysis indicates that DTI restrictions will generally impact more heavily on investors and higher-income home buyers, who borrow at higher DTI ratios on average. Our Memorandum of Understanding with the Minister of Finance on macroprudential policy requires us have regard to avoiding negative impacts, as much as possible, on first-home buyers, to the extent consistent with our financial stability objectives. We are also required to have regard to financial inclusion more generally under our Financial Policy Remit. It should be noted that lending to first-home buyers, like other borrowers, is subject to bank tests of debt servicing affordability independent of whether DTI restrictions are in place.

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Background

1. As set out in our macroprudential policy framework document[1], the purpose of macroprudential policy is to reduce systemic risk associated with 'boom-bust' credit cycles in which the financial system amplifies a severe downturn in the real economy. This in turn helps us to meet our statutory objective of "promoting the maintenance of a sound and efficient financial system" as set out in the Banking (Prudential Supervision) Act 1989.

2. The Reserve Bank's macroprudential tools are set out in a Memorandum of Understanding (MoU) between the Minister of Finance and the Governor of the Reserve Bank[2]. The tools comprise:

   - Capital/liquidity instruments: core funding ratios (CFR), the counter-cyclical capital buffer (CCyB), and sectoral capital requirements (SCR); and
   - Borrower-based instruments: loan-to-value ratio (LVR) restrictions and debt serviceability restrictions (DSRs) on residential mortgage lending.

3. DSRs were added to the macroprudential MoU in August 2021, following advice we provided to the Minister of Finance in May 2021 on policy options to support sustainable house prices. The MoU states that in the design and implementation of a DSR, we will have regard to avoiding negative impacts, as much as possible, on first-home buyers, to the extent consistent with our financial stability objectives. The Financial Policy Remit also requires us to have regard to the Government's housing policy objectives – specifically, to support more sustainable house prices, including by dampening investor demand, which would improve affordability for first-home buyers.[3]

Initial Consultation on DSRs

4. In November 2021 we issued a consultation paper[4] seeking feedback on the merits and potential design of two types of DSRs:

   - Restrictions on debt-to-income (DTI) ratios, which impose a cap on debt as a multiple of income; and
   - A floor on the test interest rates used by banks in their serviceability assessments, which test the ability of borrowers to continue repaying their loans if mortgage rates rise to a certain level.

5. Our assessment of the impacts of the two tools indicated that DTI restrictions were likely to be more effective than test rate floors in supporting financial stability and sustainable house prices, and also that DTI restrictions can be calibrated so that there are minimal impacts on first-home buyers, since first-home buyers borrow at lower DTI multiples on average while investors borrow at the highest DTI multiples.

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[1] https://www.rbnz.govt.nz/regulation-and-supervision/oversight-of-banks/standards-and-requirements-for-banks/macroprudential-policy
[2] https://www.rbnz.govt.nz/regulation-and-supervision/cross-sector-oversight/our-relationship-with-other-financial-regulators/our-memoranda-of-understanding/macroprudential-policy-and-operating-guidelines-august-2021
[3] https://www.rbnz.govt.nz/about-us/responsibility-and-accountability/our-financial-policy-remit
[4] https://www.rbnz.govt.nz/hub/news/2021/11/views-sought-on-debt-servicing-restrictions-framework

Consultation on DTI Framework

6. In April 2022, following consideration of submissions on the consultation, we announced our intention to proceed with designing a framework for operationalising DTI restrictions, in consultation with the industry and other stakeholders. Following the announcement, we held bilateral meetings with a number of banks as well as an industry-wide workshop to discuss issues related to design of the DTI framework.

7. On 9 November 2022 we published an 'exposure draft' of the framework for DTI restrictions, along with a covering consultation paper. The DTI framework consultation set out our proposed technical design rules for the implementation of DTI restrictions and invited feedback from stakeholders. We noted in the consultation that it would take around 12 months for banks to prepare their systems for the potential implementation of DTI restrictions, once the DTI framework was finalised.

8. The consultation closed on 14 December 2022 and we received seven submissions from banks, industry bodies, and members of the public. A summary of the submissions we received, along with our responses to the key points raised by submitters, has been published on our website along with redacted versions of the submissions themselves.[5] We have also published an updated final version of the DTI framework, which will now become section 20 in the Banking Supervision Handbook.

Assessment of impacts

9. This Regulatory Impact Statement (RIS) sets out our assessment of the impacts of putting in place a framework for DTI restrictions. It builds on analysis presented in the previous consultation papers (in 2017 and 2021) discussed above. The 2021 consultation paper considered the relative merits of DTI restrictions compared with an alternative debt serviceability tool – namely, a floor on the test interest rates used by banks in their serviceability assessments. On the basis of that assessment we concluded that DTI restrictions were a better tool for meeting our statutory objective of supporting financial soundness and efficiency, while having regard to supporting sustainable house prices and avoiding negative impacts on first-home buyers. We have not repeated the assessment in this document as we consider that it remains valid.

10. Accordingly, this RIS is brief and focuses on: (i) the benefits to financial stability of putting in place a DTI framework now, so that we have the option to implement DTI restrictions in the future; and (ii) the administrative costs to banks of preparing their systems for the potential implementation of DTI restrictions. We also briefly discuss the wider impacts of DTI restrictions, and provide an updated assessment of the DTI framework against the objectives in our Financial Policy Remit.

11. At this stage, we have not made a final decision on whether to activate DTI restrictions, or on the calibration of the restrictions should we decide to activate them. We intend to undertake further analysis and modelling during 2023 to inform the calibration of the restrictions, and will also consult separately on calibration prior to any final decision to

[5] https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/consultations/banks/debt-serviceability-restrictions/dti-summary-of-submissions.pdf

activate the DTI restrictions. The impacts of DTI restrictions, if implemented, will depend to a significant extent on the calibration chosen.

12. An alternative option would be not to put in place the DTI framework now, but instead to wait and assess whether DTI restrictions are needed at a future stage of the housing cycle. As will be discussed further below, this would avoid administrative costs to banks in the short term. However, there is a significant chance that if the housing cycle turns and financial stability risks begin to rise, there would be insufficient time to put the framework in place to address these risks. This is because banks have requested a lead time of 12 months to prepare their systems for the potential implementation of DTI restrictions.

Impacts on financial stability

13. Our current statutory objectives for prudential regulation under the Banking (Prudential Supervision) Act 1989 are to promote the maintenance of a sound and efficient financial system, and to avoid significant damage to the financial system that could result from the failure of a registered bank. Under the new Deposit Takers Bill (DTB), which is currently going through Parliament, our statutory purposes are proposed to change to protecting and promoting stability of the financial system, and promoting the safety and soundness of each deposit taker.

14. As noted above, our consultation on DSRs in 2021 (and prior to that, our 2017 consultation on DSRs[6]) presented extensive analysis of the potential financial stability benefits of DTI restrictions. In the 2021 consultation, we also compared the impacts of DTI restrictions to an alternative of a floor on test interest rates. We have not repeated that analysis in this RIS as we consider that it remains valid. However, in summary:

    - DTI restrictions will limit the amount of high-DTI mortgage lending on banks' balance sheets, and over time reduce the number of highly indebted households relative to the status quo. This will reduce system-wide default risk and therefore improve the resilience of the financial system to economic and/or housing market downturns.
    - DTI restrictions can help to moderate housing credit cycles by linking mortgage credit availability to incomes. This is expected to reduce both the probability and potential size of future housing market corrections, which in turn reduces the likelihood of negative feedback effects from the housing market to the financial system and wider economy.

15. Accordingly, the key overall benefit of DTI restrictions is a reduction in the likelihood of future financial crises (and/or the scale of such crises, if they occur). This in turn has benefits to the wider economy in terms of reducing potential losses in economic output. Although it is challenging to estimate the size of this benefit, academic research has found that the losses from housing-market related financial crises can be very large. Based on this literature and Reserve Bank modelling, our 2017 consultation estimated that the

[6] https://www.rbnz.govt.nz/have-your-say/closed-consultations/serviceability-restrictions-as-a-potential-macroprudential-tool-in-new-zealand

benefits of DTI restrictions could be as high as 0.25% of GDP per annum during the period they are in place.[7]

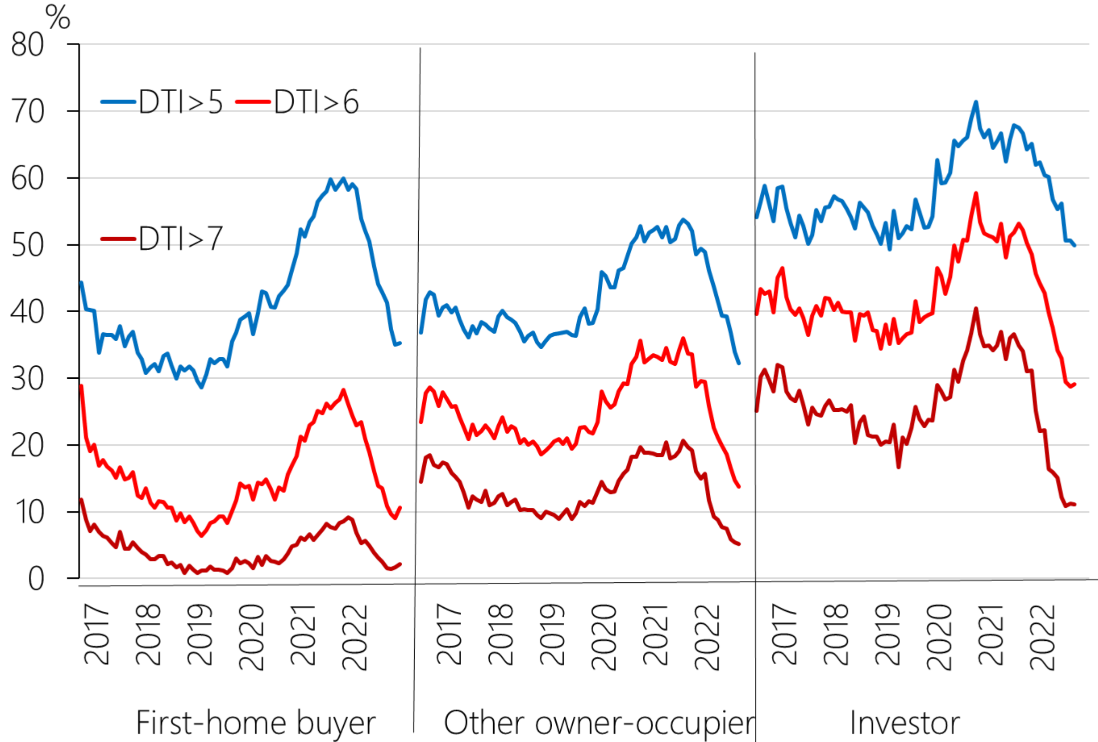
16. Our existing macroprudential regulatory tools – in particular, loan-to-value (LVR) restrictions on residential mortgage lending – also address financial stability risks related to the housing market. However, DTI restrictions address a different dimension of risk – the probability of default (PD) – to LVR restrictions, which primarily address loss given default (LGD). In addition, DTI restrictions are likely to be more effective 'through the cycle' since they link credit availability to income growth. By contrast, since LVRs of existing property automatically fall as house prices rise, LVR restrictions tend to become less binding when house prices are rising over time.

17. The housing market is currently in a downturn and borrowing at high-DTI ratios has fallen significantly in recent months, largely in response to rising interest rates (see Figure 1 below). Therefore, we do not see an immediate need to implement DTI restrictions to address financial stability risks. However, New Zealand's experience during COVID-19 shows that both high-DTI lending and house prices can rise rapidly during the 'boom' phase of housing market cycles.

18. Banks have indicated to us that they require a lead time of around 12 months to prepare their systems for the potential introduction of DTI restrictions. By putting in place a DTI framework now – and requiring banks to prepare their systems according to the rules set out in the framework – we are enabling the potential introduction of DTI restrictions at short notice in future, if they are needed to support financial system stability in line with our statutory objectives. If we do not put the framework in place now, there is a significant chance that if the housing cycle turns and financial stability risks begin to rise again, we would not be able to deploy DTI restrictions quickly enough to address these risks.

[7] Our 2017 consultation discusses these issues in more detail, and presents a high level quantitative estimate of the potential economic benefits of DTI restrictions.

Figure 1: DTI ratios by borrower type (as a percentage of lending by borrower type)



Impacts on efficiency

Allocative efficiency

19. As discussed in the 2021 and 2017 consultations, implementing DTI restrictions would create some allocative efficiency costs by impeding access to mortgage credit by otherwise creditworthy borrowers. The 2017 consultation estimated that the costs could be in the range of 0.07 percent of GDP.

20. Allocative efficiency costs can be mitigated in part through the use of speed limits and exemptions, and by adjusting the level at which the DTI cap is set. The final version of the DTI framework that we have now published includes provisions for both speed limits and exemptions. The exemptions largely mirror those for the existing LVR restrictions as set out in BS19 of the Banking Handbook. In particular:

    - Loans made under Kainga Ora's First Home Loan scheme;
    - Loan refinancing;
    - Loan portability;
    - Bridging finance;
    - New housing construction;
    - Loans granted in error; and
    - Property remediation.

21. As mentioned above, we intend to undertake further analysis and modelling and will also consult separately on calibration prior to any final decision to activate the DTI restrictions. As part of this, we will undertake a more detailed assessment of efficiency costs under different calibrations.
22. This analysis will also consider the potential interactions between DTI and LVR restrictions. It is likely that we could loosen the LVR settings somewhat if DTI restrictions were in place, while still maintaining our financial stability objectives. If so, this would reduce the allocative efficiency costs associated with LVR restrictions, thereby offsetting the efficiency costs of introducing DTI restrictions. Although more analysis is needed, it is possible that the combination of LVR and DTI restrictions could be calibrated in such a way that total allocative efficiency costs fall relative to the status quo of only LVR restrictions.
23. It should also be noted that when the new Deposit Takers Act comes into force, the promotion of efficiency is likely to be removed from our statutory objectives. However, we will still be required to take account of certain principles related to financial system efficiency, including avoiding unnecessary compliance costs and maintaining competition. In addition, the Financial Policy Remit currently states that it is desirable for the Reserve Bank to have regard to a number of Government policy objectives and desired outcomes, one of which is to have a financial system that is "strong, efficient and inclusive".

Drag on economic output

24. If DTI restrictions are activated in future, they could also create a modest drag on economic activity, since they would likely reduce the level of house prices and consumption slightly. The 2017 consultation assessed this impact using the Reserve Bank's macroeconomic model and estimated that it could be in the range of 0.1% of GDP. As with allocative efficiency costs, if LVR restrictions are loosened at the same time as DTI restrictions are introduced, this would be likely to offset some of these costs.

Compliance costs

25. Banks will need to incur administrative costs to prepare for the potential implementation of DTI restrictions. These costs include changes to IT systems and training staff on the application of the restrictions.
26. In our consultation on the DTI framework, we asked lenders if they could provide an estimate of the scale of these implementation costs. Respondents generally indicated that it was challenging to quantify costs at this stage of the process. However, based on the figures we received, we estimate that the system-wide costs of changes to IT systems could be in the range of $1.25m to $2.5m.[8] We did not receive any quantitative estimates for the costs of staff training or other implementation costs. However, we note that even if these costs were significant – for example, if the total implementation costs were in the range of $10m – this would be a small figure relative to the potential scale of both the financial stability benefits and allocative efficiency costs of DTI restrictions as discussed above.

[8] This figure is very approximate and has been derived by simply taking the cost estimates we received and extrapolating to the entire banking sector based on current market shares.

27. If we proceed to activate the DTI restrictions, there will be additional administrative costs on an ongoing basis – for example, related to monitoring and reporting. We have not attempted to quantify these costs, but expect them to be relatively low once banks' systems are in place. We note that banks already assess and report on the DTI ratios of new residential mortgage lending via the DTI survey, although aspects of the survey will change under the new framework, and banks may also need to strengthen their data collection and QA processes if DTI restrictions become a regulated requirement.

Other impacts

Impact on rents

28. In its submission on the DTI framework consultation, the New Zealand Property Investors Federation (NZPIF) expressed concern that DTI restrictions would have a negative impact on the supply of private rental properties (and presumably also lead to higher prices for such properties).

29. If and when we proceed to implement DTI restrictions, we consider that any impact on the supply of rental property will be minimal, because:

    - The design of the DTI framework incorporates an exemption for new housing construction, as well as for the remediation of existing properties;
    - The framework also incorporates speed limits, which will enable banks to undertake some lending above the DTI cap;
    - To the extent that some investors will be prevented from purchasing existing properties by a DTI restriction, this should lead to an offsetting increase in the availability of existing properties to first-home buyers who are currently renting – and consequently, a reduction in demand for rental properties from those who become owner-occupiers; and
    - To the extent that the restrictions lead to a reduction in average house prices, this will reduce the amount of debt required to purchase rental property.

Distributional impacts

30. In our previous consultations, we assessed the potential distributional impacts of DTI restrictions across different borrower groups (first-home buyers, other owner-occupiers, and investors) and household income groups. This analysis showed that DTI restrictions are likely to bind most on investors and higher-income owner-occupiers, who borrow at higher DTI ratios on average. They would bind least on first-home buyers and lower-income owner-occupiers, who generally borrower at lower DTI ratios. In addition, the DTI framework incorporates an exemption for Kainga Ora First Home Loans, which are only available to first-home buyers whose income falls below a certain threshold.

31. We note that our assessment of distributional impacts was based on data from the current DTI survey. Some definitions in the DTI survey will change following introduction of the DTI framework, and in addition, if DTI restrictions are activated, there will be a stronger

incentive on banks and borrowers to declare all available sources of income. This could lead to some shifts in the distribution of high-DTI lending, although we do not expect the general pattern to change.

32. We will undertake a more detailed assessment of distributional impacts, based on up-to-date data, prior to any decision to activate DTI restrictions. This analysis will help to inform decisions on the calibration of the restrictions. Impacts on first-home buyers are an important consideration given our requirement under the macroprudential MoU to avoid negative impacts on first-home buyers as much as possible when designing and implementing DSRs, to the extent consistent with our statutory objectives.

33. Furthermore, in response to feedback on the DTI framework consultation, we have decided to include the option of separate DTI limits for owner-occupied and investment property within the framework, as currently exist for the LVR restrictions. Although our analysis to date suggests that it may not be necessary to have differentiated limits, given that the impacts of a uniform DTI restriction are likely to bind predominantly on investors and higher-income borrowers, incorporating the option of differentiated limits into the DTI framework design will enable us to adjust the relative impacts in the future if required.

34. Another point to consider in this context is the interaction between DTI and LVR restrictions. As noted above, it is possible we could loosen LVR settings if and when DTI restrictions are in place, while still maintaining our financial stability objectives. This would benefit first-home buyers, since saving for a deposit on a first home can be challenging particularly for those on lower incomes.

35. On this point, our analysis indicates that the size of the deposit needed to purchase a first home (and the length of time required to save for that deposit) has increased significantly over the past 20 years alongside the rise in house prices. By contrast, the burden of debt servicing for new borrowers as a proportion of income has not trended higher over the past 20 years, although it fluctuates significantly at different stages of the housing cycle, as shown in Figure 2 below. This is because rising house prices – and therefore principal repayments – have been offset by a long-term decline in neutral interest rates. Consequently, introducing DTI restrictions while at the same time loosening LVR restrictions could have a net positive impact on the ability of first-home buyers to enter the housing market.

Figure 2: Indicative debt servicing ratio for new home buyers

Source: Stats NZ, interest.co.nz, Reserve Bank estimates.
Note: debt servicing costs are expressed as a share of median household disposable income and include both interest and principal repayments, based on a 30-year mortgage term and two-year fixed interest rate. Estimates are for buyers purchasing at the median selling price with a 20 percent deposit.

Assessment against Financial Policy Remit

36. The Financial Policy Remit, which was issued by the Minister of Finance on 30 June 2022 and took effect on 1 July 2022, emphasises the desirability of a strong, efficient and inclusive financial system, with a low incidence of failure of regulated entities. It also signals that we should encourage a competitive financial system and have regard to Government priorities on climate change, financial inclusion, cyber resilience and supporting sustainable house prices. The full text of the Remit is available on the Reserve Bank's website.[9]

37. We provided an assessment against the Financial Policy Remit criteria in our consultation on the DTI framework, and asked respondents whether they agreed with our assessment. Those who responded on this point were generally supportive of our assessment, although one bank stated that a test interest rate floor would achieve similar outcomes at a lower cost. In addition, the NZBA highlighted some concerns regarding the potential impact on financial inclusion of imposing DTI restrictions on top of existing lending standards, in particular the LVR restrictions and Credit Contract and Consumer Finance Act (CCCFA) regulations.

38. The table below sets out how we have had regard to the components of the Financial Policy Remit in the design of the DTI framework. It largely repeats the assessment provided in the consultation on the draft DTI framework, but updated to take account of responses to the consultation and changes we have made to the final design.

[9] https://www.rbnz.govt.nz/about-us/responsibility-and-accountability/our-financial-policy-remit

Table 1 – Assessment against Financial Policy Remit

Component of the Financial Policy Remit	Relevance with proposals in this paper
It is desirable to have a financial system that is strong, efficient and inclusive, with a low incidence of failure of entities regulated by the Reserve Bank.	The design proposals in the DTI framework will provide us with the option of introducing DTI restrictions in future. Our analysis indicates that DTI restrictions can enable help to support a strong financial system with a low incidence of failure of regulated entities.
Within the appetite of a low incidence of failure, a competitive financial system should be encouraged so as to best ensure ongoing financial efficiency and inclusion.	The design proposals in the draft DTI framework specify a consistent approach to measurement of DTI ratios across different lenders, which will help to ensure competitive neutrality. The potential impacts of DTI restrictions on financial inclusion are discussed further below.
Imposing regulatory and supervisory costs that are proportionate to the expected risks and benefits to the financial system and society.	Preparing for the potential introduction of DTI restrictions will impose regulatory costs on lenders. Wherever possible, we have adopted simple definitions in the DTI framework and used rules that are consistent with existing regulations (for example, the exemption regime for LVR restrictions) in order to minimise these costs. The estimates we received from banks suggest that implementation costs will be relatively modest in comparison to the potential financial stability benefits of having the option to introduce DTI restrictions in future.
Encouraging new investment and financial innovation that raise the productive potential of the economy.	The design proposals in the draft DTI framework are not expected to have material impacts on this element of the Remit.

Component of the Financial Policy Remit	Relevance with proposals in this paper
Encouraging the allocation of financial resources in a way that maximises the sustainable long-term growth of the New Zealand economy.	If DTI restrictions are implemented in future, we acknowledge that they will create some efficiency costs via barriers to credit access for otherwise creditworthy borrowers. As discussed above and in previous consultations, our analysis indicates that these costs would be outweighed by the longer-term benefits to financial stability. In designing the DTI framework, we have endeavoured to minimise potential efficiency costs wherever possible – including through the use of exemptions and speed limits, which allow banks discretion to continue with some high-DTI lending. The calibration of DTI restrictions (i.e. the level of the speed limit and threshold) is also an important determinant of efficiency costs. As noted above, calibration will be consulted on separately once the framework is in place. If DTI restrictions are implemented, they are expected to moderate housing credit cycles. This may help to support the efficient allocation of financial resources between housing and other sectors of the economy.
Support more sustainable house prices, including by dampening investor demand, which would improve affordability for first-home buyers.	DTI restrictions can help to support sustainable house prices by moderating housing credit cycles. DTI restrictions are expected to impact more heavily on investors and thereby dampen investor demand, as investors borrow at higher DTI ratios than other borrowers on average. In addition, the final DTI framework design allows for DTI limits to be differentiated by borrower/property type, which will provide additional flexibility to adjust the relative impact of DTI restrictions on investors versus first-home buyers if required. If implementation of DTI restrictions in future is combined with a loosening of the LVR restrictions, this could benefit first-home buyers by increasing the availability of low-deposit home loans.
Building resilience and facilitating adaption of New Zealand's economy, society and environment to climate change.	The design proposals in the draft DTI framework are not expected to have material impacts on this element of the Remit.

Component of the Financial Policy Remit	Relevance with proposals in this paper
Improving financial inclusion and maintaining financial sector diversity.	The impacts of DTI restrictions on different borrower groups will depend in part on calibration of the limits, which will be consulted on separately prior to any decision to activate the tool. Our analysis indicates that first-home buyers and lower income borrowers more generally would be the groups least affected by a DTI limit under our framework design. In addition, as noted above, DTI restrictions are expected to dampen investor demand for housing, which may improve opportunities for other borrowers to enter the housing market. The proposed exemption framework and speed limits – including the exemption for borrowers eligible for Kainga Ora First Home Loans – should further help to minimise any potential impacts on lower-income first-home buyers, and hence support financial inclusion. Furthermore, as noted above, if implementation of DTI restrictions is combined with a loosening of the LVR restrictions, this may benefit first-home buyers and lower income borrowers by increasing the availability of low-deposit home loans.
Improving New Zealand's cyber resilience.	The design proposals in the draft DTI framework are not expected to be material to this element of the Remit.

Conclusion

39. In summary, the analysis presented here, alongside our previous consultations on DSRs in 2017 and 2021, indicates that the introduction of DTI restrictions could have significant benefits for financial stability. These benefits would outweigh the potential costs of such restrictions, including allocative efficiency costs, administrative costs, and the potential drag on economic output from lower house prices and consumption.

40. At this stage, the decision we are making is whether to put in place a regulatory framework for DTI restrictions, so that banks can begin preparing their systems for the potential implementation of restrictions in future. This will incur some administrative costs, which are modest relative to the potential scale of the net benefits of DTI restrictions if they are implemented.

41. The main alternative option would be not to put the framework in place now, given that we do not see an imminent need for DTI restrictions at the current stage of the housing market cycle. This would avoid imposing administrative costs in the short term. However, given that banks require a lead time of up to 12 months to prepare for the implementation of DTI restrictions, there is a significant risk that if the housing cycle turns and high-DTI lending begins to rise again, we would not be able to implement DTI restrictions in time to address the associated financial stability risks.

42. Although we have not made a final decision on whether to implement DTI restrictions, we consider it is likely that we will use the tool in future, given the potentially large net benefits. In addition, recent experience shows that financial stability risks can rise rapidly if the housing cycle turns. Given the lead time banks require to prepare their systems, it makes sense to incur the administrative costs of putting in place the regulatory framework now, rather than deferring this to a future point in time.