

HomeStart Finance

Inquiry into home ownership

Standing committee on economics

June 2015

Executive summary

HomeStart Finance, a South Australian government agency which has helped more than 66,000 households into home ownership over almost 26 years, assists a large portion of 'would-be' home buyers underserved by the private market.

These buyers, typically on low-moderate incomes, require home finance which overcomes barriers to home ownership, such as deposit, start-up costs and borrowing capacity. Once assisted, the vast majority become reliable payers, with many quickly building enough equity in their home to refinance with a major lender.

From our experience based on creating such home ownership opportunities, we recommend the following:

- Any policy approach to address home ownership consider the impact of access to finance, and the positive role government-assisted provision of home loans to those underserved by the private market can have in overcoming the challenges facing first home buyers in particular.
- Replicating an assisted-home finance model at a national level be considered, with HomeStart's experience showing such assistance provides a pathway from rental to unassisted home buyer.

Introduction

HomeStart Finance welcomes the opportunity to make a submission to the Standing Committee on Economics' inquiry into home ownership.

HomeStart is a South Australian government agency committed to making home ownership possible for more people, particularly those underserved by the traditional lending market. For almost 26 years, HomeStart has assisted a cross-section of the state's community to overcome common challenges of securing suitable home finance. For further details, refer Appendix A.

Through adopting a prudent, adaptable and inclusive approach to managing credit risk, we have:

- helped more than 66,000 households achieve home ownership
- generated a profit every year of operation
- returned more than \$440M to the SA government since inception
- assisted approximately 1 in 8 South Australian first home buyers.

HomeStart provides home finance as a means to move people along the housing continuum from renting to assisted-home ownership (refer Appendix B for details) and, when sufficient equity has been built, to unassisted home ownership financed by the private market. More than 80% of our customers would have been unable to get a loan from a mainstream lender, and in this way home ownership outcomes through HomeStart represent genuinely improved outcomes.

Our approach has improved access to home ownership by:

- offering low deposit options (starting from 3% of property purchase price for eligible buyers)
- removing Lenders Mortgage Insurance (LMI) charges, and self-insuring our credit risk, allowing us to accept a much lower Loan Provision Charge
- accepting alternative income sources, such as Centrelink benefits and casual wages (subject to eligibility criteria)

- creating shared-equity and subsidised loans which greatly improve borrowing capacity without compromising household cash-flow.

We believe offering this bridge from rental to buying in the private market represents a sound policy instrument by which government can help bring the Australian dream of home ownership to fruition, along with the myriad of associated benefits such as increased wellbeing, stability, community connection and financial security.

About this submission

HomeStart understands that the inquiry was established to investigate the core issue of home ownership affordability primarily from the perspective of demand and supply, along with tax policy.

While we respect these issues are of high importance, we urge the Standing Committee to also consider the impact of access to affordable, sustainable home finance as an essential component of ensuring home ownership remains within the reach of Australians on low to moderate incomes. HomeStart's experience shows that the market does not meet the needs of all, and that our role in the market is one that complements the mainstream rather than competes.

This submission therefore focuses primarily on the Terms of Reference (TOR) points 2 – "Demand and supply drivers in the housing market", and point 5 "Opportunities for reform", from the perspective of our experience as a provider of home finance and with our significant knowledge of first home buyers.

Response to terms of reference

TOR – Demand and supply drivers in the housing market

Our position is that increasing accessing to affordable housing finance enables more people to buy a home than otherwise would.

The demand for home ownership has remained constant for many years, particularly amongst would-be first home buyers. Our research has found that the majority of this segment think home ownership is 'very important' (60%), primarily for financial security, however an even greater majority think it is harder to buy a home now than 12 months ago (69%).¹

The primary reasons hindering these aspiring home owners are both financial (deposit, start-up costs), and inability to borrow enough to buy a home in their price range – which can be attributed to both supply of housing priced in the low-moderate range, and securing enough funds to make a purchase.

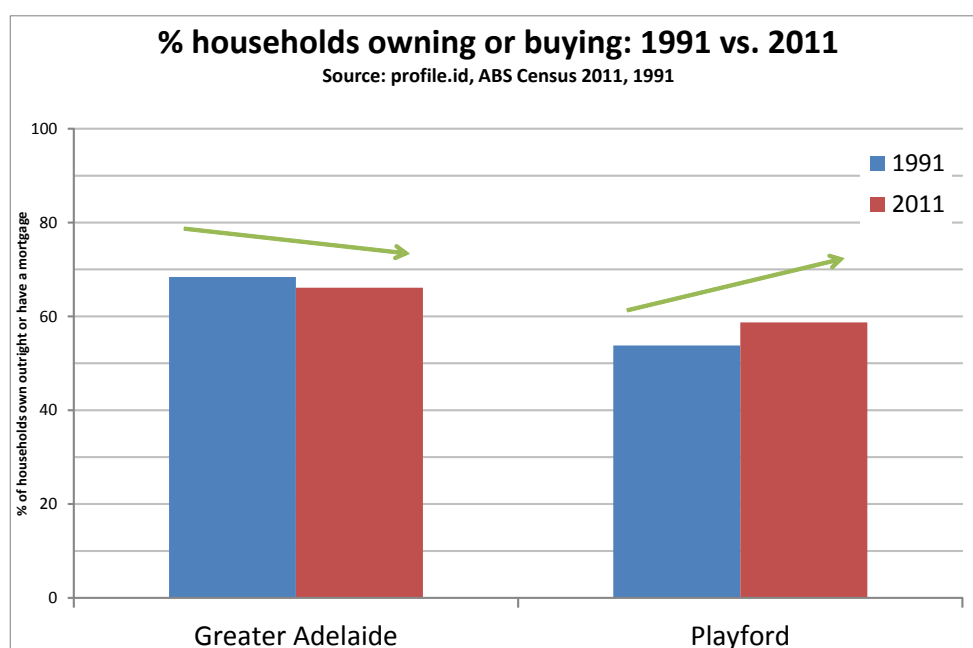
Would-be home buyers facing such issues represent a growing proportion of the potential buying market. While supply issues certainly prevent some from purchase, another sizable portion could become sustainable, wealth-building home owners if they could find suitable home finance.

An approach that addresses both supply side and affordable finance can significantly lift home ownership rates, but requires concerted collaborative effort to take effect. An example of what can be achieved with a variety of housing policies can be found in the City of Playford local government area. Playford is a broad constituency across the outer northern suburbs of Adelaide with a mixture of residential, industry and agriculture, notably including the Holden manufacturing operations at Elizabeth and RAAF Edinburgh.

¹ HomeStart's 'Home Truths' research of 499 South Australian first home buyers (2015)

The graph below shows the change in home ownership rates in Greater Adelaide compared with Playford between 1991 and 2011. Home ownership in Playford in 1991 was at 53.8% of households, compared to 68.4% for Greater Adelaide. By 2011 the gap had narrowed with Playford reporting home ownership of 58.7% (+4.9 pp) and Greater Adelaide 66.1% (-2.3pp).

This change was a function of a variety of government policies fostering home ownership including the presence of HomeStart, first home buyer grants, relatively affordable land releases and urban renewal programs. It is the combination of both affordable supply and access to finance for the intended demographic which has helped lift home ownership in this area.



TOR – opportunities for reform

Our position is that the rate of home ownership across Australia could be improved by governmental facilitation of a national program aimed at increasing access to affordable home finance.

Nationally, affordable housing policy typically leaves the provision of finance entirely up to the private sector. HomeStart’s experience and results demonstrate there is a role of government to play in providing a stepping stone for customers to move from private rental or other accommodation into assisted home ownership.

The success of KeyStart in Western Australia provides further evidence of a need for such assistance. Both programs are constrained to operating within their respective states, and not unreasonably so given the states provide capital and ongoing funding. The consequence of this limitation is that the vast majority of Australia’s population is unable to access a valuable pathway to home ownership.

Given this, we recommend that serious consideration be given to the extension of such programs at a national level. Considering that HomeStart helps approximately 1 in 8 first home buyers in South Australia alone, if this were extrapolated across the more populous states of Victoria, NSW and Queensland, the net positive and social impact across Australia would be significant.

Replicating a HomeStart-style model would require Commonwealth support around funding and capitalising lending operations, however the historical experience and data collected by HomeStart and KeyStart would provide plentiful expertise with which to devise similar programs.

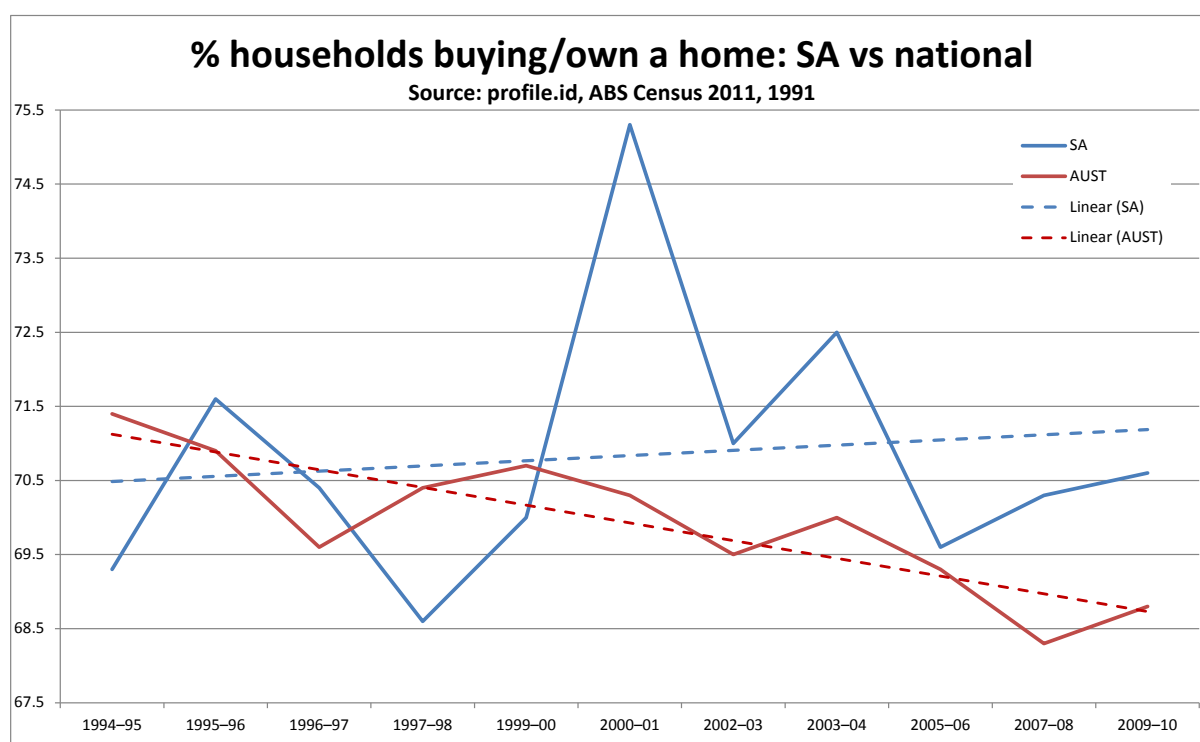
Further, the risk to government of offering such finance has proven to be minimal. While the lending profile of HomeStart's customers may not be attractive to mainstream lenders, evidence suggests it does not represent unmanageable risk. In fact, independent research based on economic modelling conducted by AHURI² examines whether government taking on such risk is tenable in the long term for both the home buyer and the program supporting them, concluding that:

Successful homeownership programs create a wealth of social benefits while reducing government spending through encouraging greater individual and private institutional investment in housing.

It also notes that:

Most directly these [research] findings suggest both the need for, and the potential effectiveness of, homeownership assistance schemes that target low-to-moderate income earners...there is a strong argument for expanding the national coverage of such Programs...

As further evidence as to the potential impact of providing assisted-home finance, census data shows that the linear trends in home ownership rates in South Australia have defied the national trend toward decline. While supply and affordability would play a role in this trend, we believe affordable finance has a role to play and is one policy lever government can utilise to positive effect.



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² Greive, S et al (2006) 'Falling through the net? A risk management model for home ownership schemes', retrieved from AHURI online.

Appendix A – HomeStart background

HomeStart Finance was established by the SA government in 1989 with the purpose of operating a home ownership assistance program. In nearly 26 years, HomeStart has now helped an entire generation of South Australian home buyers to purchase a home, generated a profit in every year of operation and returned more than \$440M to the SA government. It is estimated that more than 80% of customers would have been unable to get a loan from a mainstream lender at the time they purchased a home. The organisation's current loan portfolio is approximately \$1.85bn, supported by net assets of around \$178M.

HomeStart's reason for being is to "make home ownership a reality for more people in more ways" and this is achieved by:

- Accepting a wider range of customer income sources for loan servicing, including Centrelink benefits
- Accepting lower deposits for certain groups of customers, such as people with formal qualifications. By way of example, a customer with otherwise good credit standing and holding a Certificate III qualification or higher is able to purchase a home with a 3% deposit.
- Increasing customer borrowing power without increasing monthly instalments, through subsidised rate home loans or innovative structures such as shared equity
- Reducing upfront costs through self-insuring the credit risk on its mortgage portfolio, enabling customers to avoid paying lenders mortgage insurance (LMI) and instead pay a loan provision charge which for most borrowers is much smaller than LMI

Legislative context and governance

HomeStart is a statutory corporation established under the South Australian *Housing and Urban Development (Administrative Arrangements) (HomeStart Finance) Regulations* pursuant to the *Urban Renewal Act 1995*. HomeStart is empowered to:

- Facilitate home ownership in South Australia by lending and providing other forms of financial assistance, including finance on concessional or special terms for low to moderate income earners.
- Provide, market, and manage home finance products and facilitate schemes to encourage home ownership, including mortgage relief schemes, as well as facilitating finance for the development of aged care facilities and rental accommodation in regional areas.

HomeStart is administered by an independent, seven member Board of Management, which is responsible to the Minister for Housing and Urban Development for overseeing business operations.

HomeStart operates as a financial institution and complies with relevant consumer credit legislation including the *National Consumer Credit Protection Act 2009 (Cwlth)* which governs the licensing and supervisory regime for brokers and lenders.

The organisation is also subject to a range of other legislation including the *Privacy Act 1988 (Cwlth)* and the *Anti Money Laundering and Counter Terrorism Financing Act 2006 (Cwlth)*.

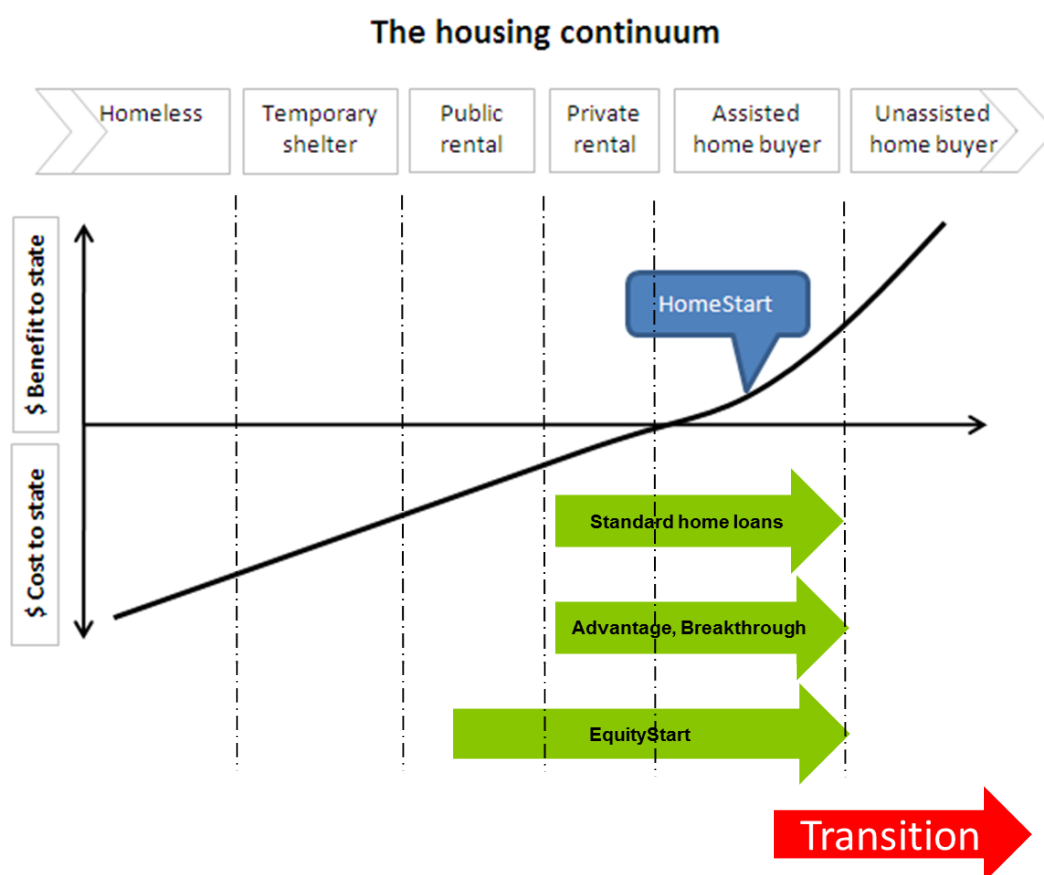
Competitive neutrality

Lending activities are financed by the South Australian Financing Authority (SAFA) at market rates and HomeStart operates within an overall borrowing limit agreed with the SA government. Consistent with the principles of competitive neutrality a guarantee fee of 1.60% is paid on outstanding debt and HomeStart's current variable interest rate of 5.54% is priced above the market average. HomeStart does not offer any rate discounts.

In this way, HomeStart uses its interest rate deliberately to position itself as an interim solution for customers entering home ownership for the first time or re-entering the market after changes in their life circumstances.

Appendix B: Role in the SA housing finance market

HomeStart's role in the home finance market is best described using the housing continuum diagram below, illustrating the different housing tenures and corresponding cost / benefit to the state.



The diagram shows how HomeStart's products are targeted at people in private or public rental and enable them to shift to the right, moving away from government assistance including Commonwealth Rent Assistance (CRA). It also highlights that home ownership via HomeStart provides a net financial benefit to government, as opposed to the cost of services through provision of public rental (e.g. HousingSA), private rental assistance (e.g. CRA) or resulting from homelessness.

A key message from the housing continuum is that HomeStart is the gateway for customers to eventually achieve home ownership via mainstream finance. To this end, HomeStart positions itself as a way to buy a home sooner, and also as an interim step between renting and home ownership.

This means customers who discharge their HomeStart loan (either by repayment or to refinance to another lender) represent successful home ownership policy outcomes.

At times in the past HomeStart has proactively worked to refinance customers to other lenders. Strategic levers – an interest rate higher than market, use of brokers for distribution – are used to achieve this goal in the long run.