



**Residential**

## **HOUSING AFFORDABILITY SUBMISSION**

**Presented By;**

**Anthony Kinder  
General Manager**



## **Submission on Housing Affordability**

BGC (Australia) is a privately owned construction, construction materials and civil contracting organisation. In 2003, BGC through its acquisition of a further 50% in J-Corp became Australia's largest homebuilder with an annual production of around 4,000 dwellings.

BGC's project housing operations range from entry level housing for first homebuyer's through to executive level two storey residences and include the following brands; Statesman Homes, National Homes, NOW Homes, Commodore Homes, StrataWise, The West Australian Housing Centre and GO Homes. With the acquisition of J-Corp, BGC now also includes Perceptions, Impressions, and Homestart.

The company's founder Len Buckeridge has been a visionary for housing affordability in Western Australia for over 40 years since winning the James Hardie architectural prize for his final year thesis in architecture "the economical house" through to receiving the industry's highest accolade, the HIA Sir Philip Lynch Award for services to the housing industry.

### **Introduction**

This submission focuses solely on the first home buyer, and their ability to finance the purchase of a house and land package at current prices in Western Australia.

The submission leaves the complexities of the local, state and federal government taxes, charges, infrastructure and planning issues to bodies such as the Housing Industry Association (HIA) and Urban Development Institute of Australia (UDIA) who have already presented fully researched submissions to the Inquiry. For its part, BGC Residential supports the arguments put forward in both the HIA and UDIA submissions.

### **Executive Summary**

Based on lending criteria of both a major mortgage broker and Keystart (the Western Australian State Government lending body), the Western Australian (WA) household earning an average income and qualifying for the First Home Owner's Grant can now only afford between 65% and 86% of the purchase price of the most affordable house and land package in the Perth metropolitan area excluding stamp duty and fees<sup>1</sup>.

While the proposed changes to lending criteria outlined in the paper do not necessarily bring the average WA family up to the point where they are able to afford the median house and land package, they are able to purchase price the most affordable house and land package, and indeed have the ability to finance packages that approach the median in price.

### **The 'Average' Western Australian Household**

The 2001 Census shows that 70.7% of households in Western Australia were either owned, or in the process of being owned. Of these owner occupied private dwellings, some 224,865 (46.9%) were inhabited by couples with children and 173,471 (36.1%) were inhabited by couples with no children.

---

<sup>1</sup> Calculations based on a couple without children excluding Family Tax Benefit A & B. Figs contained table 1 and 3.

Average Weekly Earnings (AWE) in Western Australia were \$706.00 per week gross which equates to \$36,712 per annum gross and takes into account casual and part-time earnings. Average Weekly Ordinary Time Earnings (AWOTE) in Western Australia were \$918.40 per week gross which equates to \$47,757 per annum gross and reflects full-time earnings only.

At the time of writing, the cheapest house and land package that is on offer is worth \$131,650 (73.6m<sup>2</sup> home). The cheapest house and land package that qualifies for Keystart assistance is \$143,500 (91.4m<sup>2</sup> home) as Keystart have a covenant of a minimum 90m<sup>2</sup> living area before a loan will be considered. The median house and land package in the metropolitan area is \$251,285. The median house price for an established home in Perth is \$236,000.

The examples presented below utilise the above demographics to highlight the availability of finance for the average first home buyer in Western Australia.

### Standard Lender (excluding Keystart)

Most lenders begin by stating that they will lend up to 95% (and in some instances 98%) of the value of the house and land package. The maximum allowable loan for each household is determined by a mix of the deposit that can be offered on the loan and a sliding multiplier of household income (in most instances, the smaller the income, the smaller the multiplier). What qualifies as assessable income varies between each lender with most allowing only a percentage of commission income, Centrelink payments, casual and part-time income in their calculations.

All lenders require the borrower to take out mortgage insurance for loans above 80% of the value of the house and land package. For most first home buyers, the mortgage insurance premium is around 2% of the total value of the loan. Not all lenders allow for this premium to be added to the loan, and it poses yet another barrier to the first home buyer.

The example below uses the lending criteria supplied by Wizard Home Loans as they had the most generous treatment of the FHOG (excluding Keystart).

**Table 1**

	<b>Couple No Dependents</b>				<b>Couple Two Dependents</b>			
	<b>AWE (\$36,712)</b>		<b>AWOTE (\$47,757)</b>		<b>AWE (\$36,712)</b>		<b>AWOTE (\$47,757)</b>	
	<b>Cheapest</b>	<b>Median</b>	<b>Cheapest</b>	<b>Median</b>	<b>Cheapest</b>	<b>Median</b>	<b>Cheapest</b>	<b>Median</b>
House and Land Package	\$131,650	\$251,285	\$131,650	\$251,285	\$131,650	\$251,285	\$131,650	\$251,285
Max Loan Amount	\$80,471	\$114,643	\$80,471	\$114,643	\$75,522	\$75,522	\$80,471	\$114,643
Deposit Held (2% pp)	\$2,633	\$5,025	\$2,633	\$5,025	\$2,633	\$5,025	\$2,633	\$5,025
FHOG	\$7,000	\$7,000	\$7,000	\$7,000	\$7,000	\$7,000	\$7,000	\$7,000
Monthly Repayments	\$554 (18%)	\$790 (26%)	\$554 (18%)	\$790 (26%)	\$520 (17%)	\$520 (13%)	\$554 (18%)	\$790 (26%)
Deposit Gap	\$41,546	\$124,617	\$41,546	\$124,617	\$46,495	\$163,738	\$41,546	\$124,617
<b>% of House and Land Package</b>	<b>68%</b>	<b>50%</b>	<b>68%</b>	<b>50%</b>	<b>65%</b>	<b>35%</b>	<b>68%</b>	<b>50%</b>
Term	25 years	25 years	25 years	25 years	25 years	25 years	25 years	25 years
Interest Rate (Ezibuild)	6.72%	6.72%	6.72%	6.72%	6.72%	6.72%	6.72%	6.72%
Mortgage Insurance	\$1,609	\$2,293	\$1,609	\$2,293	\$1,510	\$1,510	\$1,609	\$2,293

At AWE and AWOTE, the amount of deposit is the primary determinant of whether the household qualifies for a Wizard Loan and so loan amounts are the same. The maximum loan amount drops to \$75,522 when the AWE household has two dependents.

In the table above, each household qualifies for a loan only because the FHOG is accepted as a full deposit. In the absence of the FHOG, the household does not qualify for a loan with a 2% deposit. Indeed, they would need to have at least a 10% of the purchase price as a deposit in order to be considered for a loan. In practical terms, most first home buyers entering the market typically have a deposit of \$2,000 making it near on impossible for the average WA household to qualify for a loan without government assistance.

In the AWE example, \$2,633 provided by the household plus \$7,000 FHOG gives a deposit of \$9,633 on the cheapest house and land package. This is considered to be equal to a 7.3% deposit which enables the household to borrow \$80,471. In order to qualify for a loan amount that would enable the household to purchase the cheapest house and land package, a deposit of 5% of the purchase price, plus the FHOG is required.

## **Keystart**

Keystart is Western Australia's state government backed lender, whose charter is to assist low income families with home ownership.

The Keystart mission statement reads:

***"Based upon a foundation of integrity and respect for the individual, Keystart enables Western Australians on low to moderate incomes and low deposit borrowers to own their own home by offering an affordable loan package which also satisfies the social and financial responsibility of the Government of Western Australia".***

As of June 2003 it accounted for 21% of first home buyer approvals (both established and new homes) in WA.

Features of the Keystart loan include:

- 2% or \$2,000 deposit (whichever is greater)
- Maximum purchase price of \$250,000,
- Maximum loan amount of \$240,000,
- Interest rate on standard variable of 6.99% p/a.
- Maximum Assessed income limit of \$85,000 (per applicant)
- Maximum loan size is determined according to income as follows:

For Incomes equal to or less than \$35,000 p/a:

- The annual loan repayments cannot exceed the Debt Service Ratio (DSR) of 27% of the assessed annual income.
- Total annual commitments including the loan, other loans, credit cards cannot exceed 33% of the assessed annual income.

For Assessed incomes greater than \$35,000 p/a and below \$43,000 p/a:

- The maximum DSR for the loan and total commitments varies according to the applicant's number of dependents:

**Table 2**

<b>Applicant</b>	<b>Loan (DSR)</b>	<b>Total Commitments (DSR)</b>
Couple/Single	31%	35%
+1 Dependent	30%	35%
+2 Dependents	29%	35%
+3 Dependents	28%	33%
+4 Dependents	27%	33%

Assessed incomes equal to or above \$43,000 p/a:

- The annual loan repayments cannot exceed the Debt Service Ratio (DSR) of 31% of the assessed annual income.
- Total annual commitments including the loan, other loans, credit cards cannot exceed 35% of the assessed annual income.

The DSR is calculated based on 2% above the current Keystart interest rate.

Keystart adopts a conservative assessment of an applicant's maximum borrowing capacity compared to the majority of the market offering a standard variable loan package.

- Ability to use FHOG of \$7,000 as deposit and to cover purchasing fees
- More flexible in determining assessable income eg include child maintenance payments, family tax benefit etc
- Does not require mortgage insurance
- Minimum house size of 90m<sup>2</sup>
- Requires minimum building standards including (Floor Coverings, Window Treatments, Driveways).
- Fee assistance is provided for non-first homebuyers up to \$2,000 as part of the loan amount.
- Keystart does not charge any management or account keeping fees.

The Keystart interest rate has historically been marginally lower than the standard variable interest rate offered by the major banks. At present Keystart's rate is 6.99% p/a compared with the major banks rate of 7.07% p/a.

In the standard variable market, Keystart's interest rate combined with no mortgage insurance or ongoing fees does offer the lowest comparison rate presently available in the market place.

A current median house and land package in excess of \$250,000 precludes households from applying for a Keystart loan.

**Table 3**

	<b>Couple No Dependents</b>		<b>Couple Two Dependents<sup>2</sup></b>	
	AWE (\$36,712)	AWOTE (47,757)	AWE (\$36,712)	AWOTE (47,757)
<b>House and Land Package</b>	<b>\$143,500</b>	<b>\$143,500</b>	<b>\$143,500</b>	<b>\$143,500</b>
Max Loan Amount	\$113,100	\$140,630	\$138,400	\$140,630
Min. Deposit (2% pp)	\$2,870	\$2,870	\$2,870	\$2,870
Family Tax Benefit A & B p.a.	Nil	Nil	\$8,237	\$5,110
FHOG	\$7,000	\$7,000	\$7,000	\$7,000
Monthly Repayments	\$799 (26%)	\$994 (25%)	\$978 (26%)	\$994 (23%)
Deposit Gap	\$20,530	Nil	Nil	Nil
<b>% of House and Land Package</b>	<b>86%</b>	<b>105%</b>	<b>104%</b>	<b>105%</b>
Term	25 years	25 years	25 years	25 years
Interest Rate	6.99%	6.99%	6.99%	6.99%
Mortgage Insurance	Nil	Nil	Nil	Nil

At AWE and AWOTE, the level of household income is the primary determinant of qualification. The maximum loan amount does not change when the household has two dependents.

At AWE, the absence of the FHOG results in a deposit gap of \$27,530, reducing affordability to 81%. At AWOTE, the absence of the FHOG still results in affordability in excess of 100% (102%), ie the household can still borrow enough to purchase the minimum house and land package considered by Keystart.

### **Possible Solutions**

Notwithstanding the arguments being put forward by the HIA and UDIA in relation to reducing the overall cost of a house and land package due to government fees and charges, it is also beneficial to look at the 'access to funds' side of the equation.

#### **Monthly Repayment Capacity**

The Department of Housing and Works has a stated goal of keeping a household's rental payment to 30% of gross income.

If a similar approach is taken to lending for house and land packages at current rates, a household on AWE could increase its borrowing capacity to \$129,800 and a household on AWOTE could increase its borrowing capacity to \$168,800.

Utilizing this change alone, the % of borrowing to the house and land package closes to 90.5% and 117.6% alone.

<sup>2</sup> To the financial year ended 30<sup>th</sup> June 03, only 29.6% of West Australian Housing Centre clients had 2 or more children.

## **Home Loan repayment assistance in lieu of rental Assistance**

Currently Centerlink provides rental assistance while DHW provide bond assist to those looking to enter the rental market. Reviewing both of these practices could provide an incentive scheme for those wishing to own their own homes by converting the rental assistance amount into increased repayment capacity for low income earners.

Rental assistance can range from \$50 to \$180 per month. If added to the repayment capacity, an AWE household could increase their borrowing capacity significantly.

This serves two purposes;

- Encourages those households who are on the cusp of housing affordability to own their own home. Evidence would suggest that these occupiers have a greater vested interest in the value and maintenance of the property.
- Leaves the DHW stock to those in the community for which housing affordability is not likely in the near future.

## **BCA Energy Efficiency**

In mid 2003, changes to the Building Code of Australia introduced energy efficiency related criteria on new homes built in Western Australia. BGC supports these initiatives though it should be noted that the cost of materials and additional compliance is ultimately borne by the consumer.

The two main benefits of Energy Efficiency being applied to new homes are;

- At a macro level, conservation of non renewable resources in line with National and International obligations
- At a micro level, ongoing efficiency at the household level leading to lower household running costs.

To support these changes at the micro level, households compliant with the energy efficiency principles should be granted concessional interest rates to offset the initial cost and reflect the reduced ongoing running costs. Where the homeowner surpasses the minimum requirements, the concessional rate could be further increased.

A 50 basis point concession to current house and land package interest rates means that the AWE household could borrow up to \$139,290 and the AWOTE household \$181,170 where the maximum loan amount is calculated on the ability to repay.

The above example shows that by using concessional interest rates as opposed to cash back incentives (re introduction of the solar water heating initiative) add greater leverage to the home owner.

## **Review of the "Keystart Qualifying Rate Mechanism"**

Keystart use a qualifying rate of 2.00% greater than their repayment interest rate in order to determine a household's maximum loan amount.

In a period of relative interest rate stability, a 2.00% qualifying rate buffer is an impediment preventing those on average incomes borrowing amounts nearing the median house price.

In both of the above examples, the Department of Housing and Works Rental Assistance and the BCA Energy Efficiency recommendations, the cost of reducing the 2.00% qualifying rate buffer down to 1.00% or 0.50% is negligible compared to the benefits of increased borrowing power to the potential homeowner.

An option to offset the risk in the reduction of the qualifying rate buffer could be to fix the interest rate for a period of three-five years.

While these suggestions in themselves do not take all households to the point where they can afford to purchase the median house and land package in Perth, they have within their reach the packages in the lower deciles.

### **Shared Equity Schemes**

In 1997, Keystart introduced a shared equity product known as "GoodStart".

Low income earners were able to purchase a portion of the property with a minimum share of 50%. The remaining share was purchased by The Department of Housing & Works.

This model assisted the applicant into home ownership with a smaller loan requirement reflecting their equity position. The amount of equity to be taken up by the applicant would be determined from their income to ensure they achieved the largest portion possible.

The applicants would be responsible for maintenance and upkeep of the property and to pay their portion of rates and insurance costs. On sale of the property, the proceeds would be distributed according to the equity split. Any improvements carried by the owner would be valued prior to the sale and included in the proceeds to be received by the owner.

Applicants were also encouraged when their own personal circumstances permitted to purchase the remaining equity in the property.

Whilst "Goodstart" is still available today, the impact of the product is minimal as the available funding through DHW is restricted.

While there are still some inherent distractions in the "Shared Equity" models, namely the valuation of improvements at time of sale the shared equity concept still has the potential to provide a longer term solution to the housing affordability crisis.

To offer shared equity to the market will only become possible with the cooperation of financial institutions able to provide funding for that equity not able to be taken up by the home buyer.

### **Rate of Return Model**

Another variation to the Shared Equity Schemes that alleviates the problems associated with improvements during the shared equity period is the "Rate of Return Model for Financial Institutions".

This model allows home owners to enter into shared equity schemes with financial institutions on an en-masse basis, for instance a new subdivision development on a "whole of estate basis".

The financial institution contributes a standard % of the valuation of the home to a homeowner or a group of home owners in a subdivision. This is on the basis of the financial



institution receiving their contribution plus a pre agreed rate of return from the resulting sale proceeds.

This contribution is made on the basis that no interim repayments will be made by the homeowner and therefore does not increase the risk of repayment default.

In principle, both parties would benefit as the homeowners would be more likely to contribute to the ongoing maintenance and renovations knowing that they would be the recipients of the capital growth and the financial institution would have a vested interest in the maintenance of the "whole of estate" thus making the general capital growth of the area more likely.

This model is highly capital intensive however provides a suitable large scale opportunity for financial institutions to achieve rate of return requirements and building a sense of community while at the same time creating a low maintenance relationship with the homeowner.

### **FIRST HOME OWNERS GRANT – MEANS TESTING**

The First Home Owners Grant (FHOG) was established in 2000 to offset the impact of the introduction of the GST. Whilst the initial grant of \$7,000 was welcomed by the general public, the scheme was not truly effective until the revision to \$14,000.

The benefits of this Scheme are;

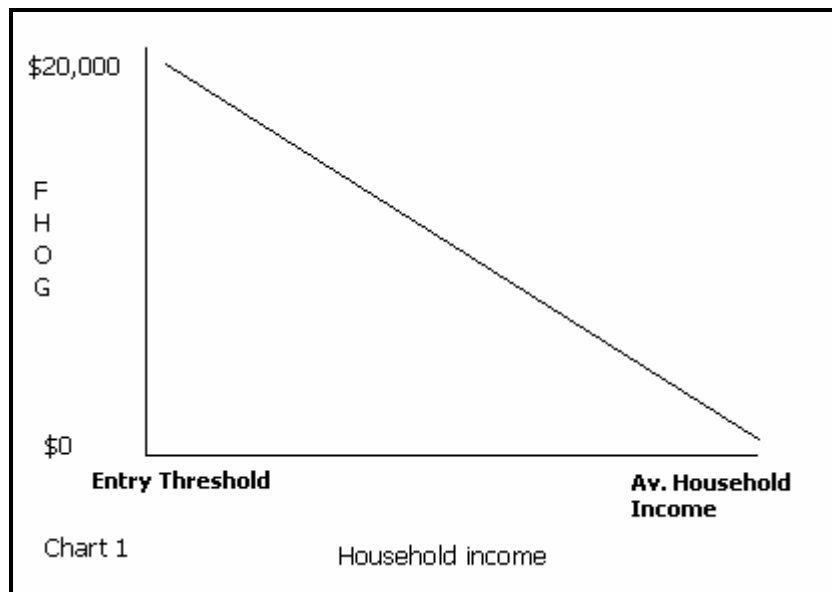
- That it is generally easy for Government to implement and maintain,
- The West Australian Government's treasury department has been active and successful in identifying those seeking to defraud the grant mechanism.
- Above all other stimulants in the past decade (other than the pull forward of the pre GST itself), the FHOG and particularly the \$14,000 for new homes has made a substantial impact on the demand for new homes.

Criticisms of the Scheme are;

- Not means tested which has led to sensationalist headlines in the media
- It is generally not available at the time of settlement when most of the recipients require it for upfront fees and charges.
- Many lenders will not allow it to be used as a deposit despite equating to just under 5% of the entry level house and land package.
- As shown in table 3, it is generally not sufficient to make a substantial difference to those who really are at the cusp of the affordability equation.

BGC Residential puts forward that the FHOG be revised on the following basis;

- Means tested so as to apply to only those only in greatest need being on or under the average household income.
- A sliding scale of the value of the grant is applied based on the level of household income, (see chart 1).



- The lower income point at which the grant would be at its maximum would be near the threshold for those able to gain entry to the lower end of the housing market.
- At the higher income point would be based on the average household income.
- In both cases, the upper and lower income points could be tailored on a state by state basis, or capital city, regional centre or regional area to allow for the deviation in house prices and incomes.
- The administration would remain relatively simple. It is suggested that the lender use the supporting loan documentation stating the owner's income as the basis for the FHOG income assessment thus creating a preventative mechanism for households to understate their income to obtain a higher grant amount.

## Conclusion

This submission clearly shows that, on current lending criteria used by both state government and private lending institutions, the 'average' WA household is being squeezed out of the first home owner's market despite the FHOG.

While cost factors such as associated with local, state and federal government taxes and charges are one side of the affordability equation, access to funds is also an issue. Government assistance in the form of changes to lending criteria, subsidies and interest rate concessions can go a long way to improving the ability of the 'average' WA household to achieve its dream of home ownership.

For further information, please contact

Anthony Kinder  
General Manager  
BGC Residential

4 / 22 Mount St  
Perth WA 6000

[anthony@bgcresidential.com](mailto:anthony@bgcresidential.com)

0413 748 700

Ref 0.06 FINAL