Home Loan Clampdown on the Cards

Australia's housing boom has continued to steam ahead over recent months. Last week, data showed that dwelling prices increased by 1.5% in September. The pace of the boom has been moderating over recent months and is down from the peak of 2.8% in March 2021. However, monthly growth is still well above the decade average of 0.4%. In annual terms, dwelling prices have increased over 20% in the year to September, marking the strongest annual growth since 1989.

Separately, credit extended for housing has continued to grow and increased at an annual pace of 6.2% over the year to August. This is the fastest annual growth in three and a half years.

The persistent strength in the housing market has prompted concerns that the price increases and credit growth are unsustainable and that action needs to be taken by regulators. The Council of Financial Regulators (CFR), which includes the Reserve Bank (RBA), the Australian Prudential Regulation Authority (APRA), Australia's banking regulator, the Australian Securities and Investments Commission, and the Australian Treasury, have been monitoring developments in the market closely. So far, they have emphasised that lending standards remain sound.

It is important to note that regulators do not target a level of housing prices. Instead, the focus is on risks to the economy from a deterioration in lending standards or excessive household debt levels, which can be associated with a rapid run up in property prices.

Recently, regulators have been sending increasingly strong signals that intervention may be required. In recent speeches, senior RBA representatives have discussed the risks to the economy from excessive household debt levels and highly leveraged borrowers. Additionally, concerns have been noted around the sustainability of household credit growing significantly faster than household income.

Last week, rhetoric stepped up a notch when it was noted that the Federal Treasurer attended the quarterly CFR meeting. This is unusual. In a statement, the Treasurer said that 'targeted and timely adjustments' may be required to prevent the build-up of future risks in the financial system. Plus, it was flagged that APRA will publish a paper on its framework for implementing macroprudential policy over the next couple of months.

At face value, these developments might not seem that significant. But for regulators, who are ordinarily very tight-lipped, these are strong statements and suggest that an implementation of macroprudential policy tools is on the cards.

Regulators have experience in implementing such tools. Over late 2014 and early 2015, limits on investor lending growth were imposed to control excessive risks from investor loans. In 2017, regulators also imposed limits on interest only lending. However, it is unlikely that these same tools will be applied this time around.

So what form are these adjustments likely to take?

The RBA gave an indication in a recent speech on the housing market. Excessive risks from highly indebted borrowers were noted as a key concern. This suggests that limits on the amount of loans that go to household with high debt-to-income ratios may be implemented. Additionally, higher serviceability requirements may be imposed on new borrowers. This would require that new borrowers are assessed using higher interest rates to ensure that they would still be able to repay loans if interest rates increase in the future. These measures would reduce the amount of debt that certain borrowers would be able to obtain.

The forthcoming APRA paper will likely step out the tools that regulators will apply.

Looking to the week ahead, the RBA will be publishing its half-yearly Financial Stability Review on Friday. This provides an assessment of global and domestic financial stability risks and an overview of current conditions in the financial system. The Review will provide an indication as to the RBA's current thinking around the housing market and may provide further clues on the form any potential macroprudential policy tools may take.

The RBA Board also meets today. The Board is not expected to make any changes today to monetary policy settings. This follows the recent changes to the bond purchase program. The Board agreed to reduce the purchases of government bonds to $4 billion per week from early September. This was a reduction from the previous pace of $5 billion per week. The bond purchase program will continue at this rate until February 2022. The Board continues to maintain it does not expect the cash rate will be raised until 2024.

Updated estimates for the value of exports and imports in August, which are used to determine the trade balance, will be released. Australia has maintained a trade balance surplus since the beginning of 2018 (43 consecutive months). This has been supported by continued strength in commodity prices, particularly iron ore. In August, we expect this run of trade balance surpluses, the longest since the series began in 1971, to continue.

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Forecasts

		2021	2022				2023
End Period:	**Close (4 Oct)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	0.10	0.10	0.10	0.10	0.10	0.10	0.25
90 Day BBSW, %	0.02	0.07	0.10	0.15	0.20	0.40	0.65
3 Year Swap, %	0.55	0.55	0.70	0.80	0.95	1.10	1.20
10 Year Bond, %	1.49	1.55	1.70	1.80	1.90	2.00	2.05
US Interest Rates:							
Fed Funds Rate, %	0.125	0.125	0.125	0.125	0.125	0.375	0.625
US 10 Year Bond, %	1.48	1.60	1.70	1.80	1.90	2.00	2.05
USD Exchange Rates:							
AUD-USD	0.7281	0.75	0.76	0.77	0.78	0.78	0.79
USD-JPY	110.93	111	112	112	112	113	113
EUR-USD	1.1621	1.21	1.23	1.22	1.21	1.21	1.21
GBP-USD	1.3610	1.41	1.43	1.44	1.45	1.44	1.44
NZD-USD	0.6969	0.71	0.72	0.73	0.74	0.74	0.74
AUD Exchange Rates:							
AUD-USD	0.7281	0.75	0.76	0.77	0.78	0.78	0.79
AUD-EUR	0.6268	0.62	0.62	0.63	0.64	0.64	0.65
AUD-JPY	80.81	83.3	85.1	86.2	87.4	88.1	89.3
AUD-GBP	0.5353	0.53	0.53	0.53	0.54	0.54	0.55
AUD-NZD	1.0455	1.06	1.06	1.05	1.05	1.05	1.07

	2019	**2020**	**2021 (f)**	**2022 (f)**
GDP, %	2.1	-0.9	0.0	7.4
CPI (Headline), %	1.8	0.9	2.8	2.4
CPI (Trimmed mean), %	1.6	1.2	1.9	2.6
Unemployment Rate, %	5.2	6.8	5.1	3.8
Wages Growth, %	2.2	1.4	2.0	2.8

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

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