New LVR rules clarified, confirmed

Greater clarification of the details surrounding new lending requirements has come today with the Reserve Bank's confirmation of its latest investor-targeted LVRs.

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by Miriam Bell

The Reserve Bank has just confirmed the new LVR rules with the release of its response to submissions received during the consultation period on them.

Back in July, the Reserve Bank announced it planned to introduce new lending requirements for those buying property – as a result of financial stability concerns.

Under the new rules, from October 1, property investors will need a 40% deposit for a mortgage loan, while owner-occupiers will need a 20% deposit.

These rules apply nationwide, which removes the requirements for Auckland investors introduced in last year's LVR requirements and standardises the regime.

There are exemptions to the new LVR restrictions, which are applicable to both investors and owner-occupiers.

The exemptions include new builds, bridging finance, re-financing existing high LVR loans, and funding for non-routine extensive repairs due to natural disaster or weather tightness issues.

Also, borrowers with owner occupied and investor collateral can use the combined collateral exemption to obtain finance up to 60% of the value of the investment properties and 80% on their owner occupied property.

However, in today's release the Reserve Bank has said it has modifying some of its proposals in response to the consultation.

Some of the existing exemptions to LVR restrictions have now been extended.

One of the extended exemptions is for new builds as the Reserve Bank wants this exemption to prevent any negative impact on the supply side due to housing shortages.

For this reason, it said widening in the scope of this exemption would be useful in assisting the financing of new dwelling construction.

This means it will now be possible to borrow for a newly-built property – as long as it has been completed within the previous six months and is bought from the developer.

The other exemption which has been extended is for funding for remediation work.

This is in response to submitter's pointing out that rental property standards have been increased around aspects of insulation.

As a result, the remediation exemption has been extending to include funding for work required to meet rental property standards – in particular new insulation standards.

In its response, the Reserve Bank has also tried to better clarify some of the issues said to have come out of confusion over how banks should apply the new LVRs.

One such issue is whether owner-occupiers buying a second home before selling their first home as intended would qualify as investors.

The Reserve Bank said customers with this intention shouldn't be treated as investors, although it would expect banks to undertake due diligence with customers whose intentions do not appear plausible.

The other area of confusion is said to have arisen in relation to the combined collateral exemption.

It has been suggested that banks are requiring customers to reduce the LVR on a portfolio of rental properties below 60% when they sell one of the properties, before the customer takes any of the proceeds of the sale in cash.

The Reserve Bank said that repaying part of a mortgage (selling one of a pool of securities) does not need to constitute a new commitment and need not be in scope for the LVRs.

However, it added that, more generally, how the proceeds are split between borrower and bank when a property is sold will depend on the mortgage contract and the policies of the bank.

Some commentators have said they believe the effect of the new LVRs will be short-lived and not as broad-reaching as might be expected.

But the Reserve Bank said they should improve bank balance sheet resilience.

This will reduce banks' mortgage loan losses and help limit the extent that credit standards could tighten in a sharp housing market downturn.

It also expects the new LVR's to have a small, transitory impact on house price inflation which will help reduce the probability and severity of any downturn at the margin.

The Reserve Bank said it will continue to monitor the rental market, but are sceptical the new LVRs will affect the rental market much.

This is because properties that are not sold to investors will be sold to owner occupiers, reducing both the supply and demand of rental properties.

Meanwhile, it seems further macro-prudential tools are still on the horizon.

The Reserve Bank confirmed that it will be investigating the case for using a debt serviceability tool with banks over coming months.

It will also be undertaking a fundamental review of prudential capital requirements for registered banks over the next year.
The possibility of introducing macro¬-prudential capital buffers will be considered as part of this process.