



Residential

Mr Lyndon Rowe
Chairman
Economic Regulation Authority (WA)
By email: publicsubmissions@erawa.com.au

Dear Mr Rowe

Inquiry into Microeconomic Reform in Western Australia – Response to Draft Report

BGC Residential prides itself not only as Australia's largest homebuilder but also as a significant provider of affordable housing solutions. It is with this in mind that we write to indicate our opposition to the recommendation proposed by the Economic Regulation Authority (ERA) to abolish the Keystart home loan program.

In the Terms of Reference provided by the then Treasurer, the ERA was not limited in its consideration parameters when providing advice to the Government as part of this Inquiry. BGC Residential believes there are three key considerations that the ERA has failed to take into account in developing the recommendation to abolish Keystart. Whilst expanded on in the attached document, these key considerations include:

1. The impact on the State Government's public housing waitlist;
2. The impact on Western Australia's rental market; and
3. A failure to fully interrogate Keystart loan default rates.

BGC Residential believes that if Keystart was abolished there would be considerable adverse consequences across the Western Australian property market which the ERA has not fully assessed, anticipated or addressed as part of its Draft Report.

Mr Rowe, please find attached a summary of the BGC Residential submission in relation to the ERA Draft Report into Microeconomic Reform in Western Australia, submitted for your consideration.

If there is any further information that is required, please do not hesitate to contact me via email kelvinr@bgcresidential.com or on

Yours Sincerely

Kelvin Ryan
CHIEF EXECUTIVE OFFICER
BGC Residential



**Inquiry into Microeconomic Reform in Western Australia – Detailed Submission on Behalf
of BGC Residential**
7 May 2014

Impact on the State's Public Housing Waitlist

In 2009-10 there were 24,136 households on the public housing waitlist, expecting a home to be built, maintained and provided to them by the State Government. In May 2013, that figure was on a downward trend with 21,162 households on the same waitlist¹. The Minister for Housing, the Hon. Bill Marmion MLA indicated that this reduction was being achieved by:

"Providing opportunity for more affordable housing for low and moderate income households, so people do not need to rely on public housing."

The success of this strategy includes the Keystart program and has resulted in a reduction of the waitlist, whilst in contrast; other State's and Territories have experienced an increase of persons waiting for public housing.

For those who had been selected from the waitlist, there were 33,896 public housing dwellings in Western Australia². The net recurrent cost per dwelling (i.e. the provision of assistance, recurrently including cost of capital, administration and operation costs) was in excess of \$37,000³.

As the ERA concedes in the opening statement of its *Overview of the Microeconomic Reform Inquiry*:

*"Keystart provides home loans to Western Australians who are unable to obtain financing from the private sector"*⁴

Since 1989 Keystart has provided finance for more than 85,000 households, and currently has a loan book with over 16,000 active mortgages.

If the ERA's recommendation to abolish Keystart was acted on, it has to be expected that by virtue of the ERA's own concession (provision of Keystart finance for those who cannot get bank finance) there would be a portion of these individuals who would have to seek public housing.

Between 1 January 2010 and 30 June 2013, Keystart has provided some 4655 new loans⁵. If Keystart didn't exist, and it was assumed that 50% of these households sought public housing assistance, the State Government would see an additional demand of at least 2327 households. A draft assumption shows that if the State Government had to build public housing to cater for this increased demand, aside from the initial capital expenditure, there would be a recurrent expenditure of \$87,006,530 on these newly built properties alone.

Unlike public housing, Keystart does not receive an allocation from Consolidated Revenue. It can also be seen that the program as part of an overall affordability strategy implemented by the Government, has resulted in a real reduction public housing waitlist.

¹ Minister for Housing, Parliament of Western Australia: Legislative Assembly Debates (Hansard) 12 June 2013

² As at 30 June 2012, Steering Committee for the Review of Government Service Provision, 'Report on government services 2013', Productivity Commission, 31 January 2013, table 16A.20.

³ Steering Committee for the Review of Government Service Provision, 'Report on government services 2013', Productivity Commission, 31 January 2013, table 16A.20.

⁴ Overview of the Microeconomic Reform Inquiry (2014), p24.

⁵ Department of Housing, Annual Report 2012-13, pg. 16

The ERA has failed to account for this foregone expenditure in public housing, both in capital and recurrent costs, which would result should Keystart be scrapped.

In the Terms of Reference provided to them by the then Treasurer, the ERA was not limited in its development parameters when providing recommendations to the Government. In so far as social policy considerations are concerned, it is clear that the ERA has failed to fully assess the social impact that scrapping Keystart would have to both the Western Australian community at large and with specific respect to the public housing waitlist.

Impact on Western Australia's Rental Market

Similar to the assumptions made above, it can be extrapolated that a cessation of the Keystart would see increased pressure on Western Australia's rental market. This impact has failed to be accounted for as part of the Draft Report issued by the ERA.

Individuals, who cannot obtain bank finance but receive a loan through Keystart, are not competing in the rental market. Abolishing the program would see a significant number of people forced into either public housing or the rental market.

For example, a family earning a combined income of \$120,000 a year is eligible for a Keystart loan (along with other more rigorous parameters that must be met). If the program was abolished, they cannot only fail to realize home ownership but they would also be forced to enter the rental market. This would see the family compete for tenancy with persons earning significantly less money and who have no other choice but to rent.

It can be considered that abolishing Keystart would place immense pressure on the rental market in Western Australia. Indeed had Keystart not existed, not only would 85,000 Western Australians have been robbed of the opportunity to own their own homes but this may have had a significantly negative impact pushing those on lower incomes out of rental accommodation and into homelessness, crisis care and/or onto the public housing waitlist. It is clear that the injection of that 85,000 cohort would have a detrimental impact on the State's finances, let alone the many social and political issues that would follow.

It is disappointing that the ERA has not explored the impact Keystart would have on the rental market. It does acknowledge Keystart:

"... has a number of potential benefits, including easing pressure on rental markets as more people transition into ownership from renting."

However the Draft Report has failed to expand on this item instead this statement is followed by the subsequent caveat:

"... it is difficult to ascertain the extent to which Keystart contributes to these outcomes"⁶

In the Terms of Reference provided to them by the then Treasurer, the ERA was not limited in its development parameters when providing recommendations to the Government. In so far as social policy considerations are concerned, it is clear that the ERA has failed to fully assess the social impact that scrapping Keystart would have on the rental market.

Keystart Default Rates

An integral assumption to the Draft Report produced by the ERA, is the that:

"The lending activities of Keystart pose an unreasonable level of risk to Government finances, reflecting the size of the Keystart loan book and the fact that Keystart clients are at higher risk of default because of their low deposit to loan ratios."⁷

⁶ Inquiry into Microeconomic Reform in Western Australia: Draft Report, pg 319

⁷ Overview of the Microeconomic Reform Inquiry (2014), p25.

The ERA has failed to look at historical default rates of those on Keystart loans, compared to private financial institutions. During the 'Global Financial Crisis' arrears for Keystart loans dropped during this period from 0.83 per cent in June 2008 to 0.38 per cent in June 2010. This compares with the private financial institution average arrears rate of 1.39 per cent during the same period⁸.

The Minister for Housing noted that such a low arrears rate would be 'the envy of financial institutions'⁹.

It is disappointing that as part of the Draft Report comparisons are made to the United States Government sponsored lenders Fannie Mae and Freddie Mac, suggesting that:

"While Keystart is not of the same scale of Fannie Mae and Freddie Mac, it does come at a risk and could lead to significant losses for the Government".¹⁰

The Draft Report fails to address default rates in the United States compared to that of Australia and Keystart specifically. Australia in Q1 of 2013 had an average mortgage default rate of 1.45%¹¹, this compares to the same time in the United States, which saw defaults at 9.7%¹². The Draft Report has also failed to demonstrate that Australia is ranked as having one of the lowest historic mortgage delinquency rates in the world.

The central element to the recommendation to scrap Keystart was the element of unjustifiable risk. In so making this recommendation, the Draft Report has disregarded these historic examples of default rates to justify it's own case. Whilst risk is inherent in all lending, it can be seen that even during times of economic contraction, defaults with Keystart have remained low.

⁸ Minister for Housing, Parliament of Western Australia: Legislative Assembly Debate (Hansard) 25 November 2010

⁹ Minister for Housing, Parliament of Western Australia: Legislative Assembly Debate (Hansard) 25 November 2010

¹⁰ Inquiry into Microeconomic Reform in Western Australia: Draft Report, pg 319.

¹¹ Australian Mortgage Delinquencies, Fitch Ratings Agency, 2013

¹² Board of Governors of the Federal Reserve System.