The Deloitte Australian Mortgage Report 2016
Executive summary

An extract from Australian Mortgage Report 2016

EXECUTIVE SUMMARY

Mortgages 2016: Deliver tomorrow, today?

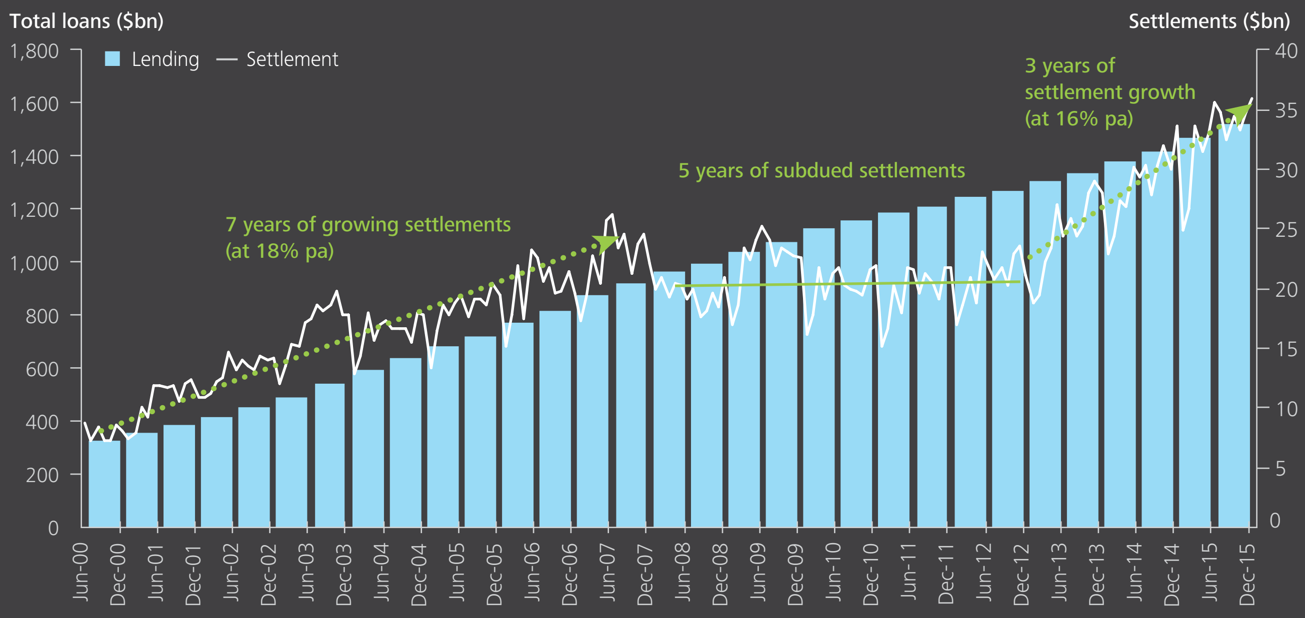
The Australian mortgage market continues to deliver. In October 2015 the total market for outstanding residential mortgages in Australia burst through the $1.5 trillion mark, with annualised lending growth of more than 7% p.a. for 2015. Settlements reached a record of almost $36 billion ($35.95bn) in December 2015 and mortgages continue to account for more than 60% of our major banks' earnings.

The total market, together with monthly settlements, is shown in the residential mortgage lending – 2000-2015 chart below.

The chart shows the historical performance of mortgage lending growth. There was a clear 'ramp up' in settlements leading to the Global Financial Crisis. During the five year period from December 2007 to December 2012, mortgage settlements plateaued as households took stock of their situation and waited to see where the Australian economy would move.

Reassured with record low interest rates and employment prospects, especially in capital cities and for higher income earners, the mortgage lending market picked up and has shown strong growth from 2013 to today.

Residential mortgage lending 2000-2015



Putting the recent growth into context against long term metrics:

- The official cash rate is at 2% as at March 2016, compared with 6% in June 2000
- Unemployment is around 6% as at March 2016, a similar level to that in 2000
- Inflation is at similar levels in 2016 compared with 2000, at around 2-2.5%.

These fundamentals give confidence in mortgage lending decisions to customers, as well as lenders. While the debt to income ratio is the one metric to have deteriorated, from around 125% in 2000 to more than 180% in 2016, this is against a backdrop of interest rates being substantially lower. This debt burden is being disproportionately shared by higher income households.

From a systemic risk perspective, Australian banks have had to increase their mix of deposit funding to ensure greater liquidity and sustainability than in 2000. Recently capital levels have been the focus as has greater enforcement of responsible lending standards.

So if the mortgage market is growing strongly and there are positive fundamentals, where are the challenges of what tomorrow will bring, and can they be addressed today?

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Deloitte Mortgage Report roundtable

We asked a roundtable comprising the heads of mortgage lending from major, regional and non-bank lenders, brokers and, this year, fintechs, to give us their views on the challenges ahead.

Customer – while a mortgage is a product, the delivery and interaction with the customer is a service. In a world where the average consumer is more technologically enabled than ever before, it is an ongoing challenge to adapt service models to meet the expectations of consumers. So what will these expectations be, and when and how will consumers give lenders the right to engage with them?

A key insight from our roundtable is the timing and type of service engagement with mortgage customers. No longer can a lender expect to wait for the customer to approach them about the mortgage product; the customer expects to be engaged in their exploration stage, in their property search stage, and their aspirational saving stage. They want service delivery to match. Once the mortgage is taken out, customers have ongoing needs around the property which go over and above the mortgage product. So how can lenders meet these expectations and differentiate? That is a challenge for tomorrow, today.

Distribution – the evolution of the broker channel is one of the glowing success stories of the past 15 years. This highly personal channel has brought the consumer a service which is valued and sought after, and should continue to be so.

However if up to 50% of all mortgages are written through a broker, where are the other 50% being written? It is not likely to be in the traditional branch. It will increasingly be digitally – but what exactly this encompasses, is the challenge for lenders. Is it a straight through end-to-end mortgage service? Is it a hybrid digital and call/mobile/video enabled support? Is it omni-channel? All these questions will be being tested by the majors looking at the way the distribution preferences of customers are evolving.

Scale – while the early 2000s was marked with increased providers, recently scale is the focus. We have seen increasing vertical integration of brokers and lenders, the pressure on smaller regional players and credit unions to merge to remain relevant, and most recently the pressure on the non-bank and mortgage manager providers to survive.

With the constant pressure to invest in technology, to develop more sophisticated risk systems, to source and manage capital, and raise sustainable funding, scale will be the enabler. However with scale comes the risk of losing nimbleness and agility – especially for customer service. This is the challenge in the race for scale.

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Fintechs – decreasing customer friction and enhancing innovation is the fintech promise. And to a growing degree we are seeing some of this disruption in the payments and personal lending space in Australia, albeit this is still in relative infancy.

What then for mortgages? This product and the service around it, is the largest single financial commitment a household will make.

The sheer size of the relative funds being advanced, the risk being borne by the lender (and subsequently investors and shareholders) and the regulatory framework, means it is not so easy to disrupt end to end. However, a question to address include the 'sandpits' needing to be carved out, or the partnerships put in place to enable fintech development in mortgages.

This will be a combined opportunity for lenders, technology providers, fintechs and regulators to work together. The promise holds much more for tomorrow, than we are seeing today.

…and the role of housing wealth

Lastly, it has been a fascinating period entering 2016 and being part of the very public discussion about the role of housing wealth for Australians and the equitable treatment of the benefits for those able to own, or take out a mortgage on a home.

The home – the principal place of residence – has long held a sacrosanct position for Australians. It is both a home in which to raise the family, and a wealth creation asset.

From the principal place of residence not being included in pension eligibility testing for retirees, nor incurring any capital gains tax on sale, to investment properties providing negative gearing benefits for investors to offset broader tax liabilities together with concessional capital gains tax treatment, property has many financial advantages afforded to Australians at all stages of life.

However, so too have other investment options. Superannuation savings have tax concessions and threshold exemptions which make it a favourable place for investment. Other broader tax related aspects around property such as land tax and stamp duty also exist.

So in these discussions about the role of housing and its benefits, there needs to be a consideration of all of these aspects in totality, rather than isolating the discussion to focus on one particular treatment.

This is a discussion which Deloitte encourages and we believe brings to light the very important role which housing and mortgages play for the Australian economy and Australian households as a whole.

In the following pages we trust you will find our 2016 Deloitte Australian Mortgage Report thought provoking, as well as an enjoyable and interesting read.

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