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Reserve Bank approved to use debt to income ratios

The Reserve Bank of New Zealand has announced plans to add debt to income ratios to its tool kit to dampen investor demand for properties.

"This will not help the supply of houses, approximately 84% of which are provided by private landlords" said Sharon Cullwick, executive officer of the NZ Property Investors' Federation (NZPIF).

The debt-to-income (DTI) ratio will limit the amount a person can borrow from between five to seven times their income. This, along with other changes that the Government has made to the removal of mortgage interest tax deductibility and loan to value restrictions (LVR's), will make it even harder for private rental property providers to supply homes for tenants. Tenants again will be the losers.

Notably DTIs reduce the likelihood of mortgage defaults while LVRs largely reduce losses to banks if borrowers' default. However, throughout the consultation period NZPIF will continue to outline the negative effects of these policies on the supply of rental properties and therefore the effect on tenants looking for homes.

Debt to income ratios will also affect those on high incomes who have borrowed significantly more than seven times their income on owner occupier homes. Overseas investors who are often omitted from these policies will also be affected. The Minister of Finance does not want debt to income restrictions to affect first home buyers. However, these may have a large effect on younger people who are starting their careers normally on lower salaries.

Constant changes in legislation will not give confidence to property investors or developers to begin building new houses to help increase supply.

The aim of all these recent changes has not been to reduce house prices but to ensure these are at a sustainable level over time, taking into account housing supply and demand, population growth, building costs, land supply and interest rates. However, if sales demand drops dramatically this may have a negative effect on prices.

The Reserve Bank of New Zealand has said it will take six months for them to assess whether the recent housing policies have taken effect and sustainable house price increases are being achieved.

Consequently, interest only loans have been removed as a tool for stopping the housing market for the time being as the expectation is that it will have little impact on slowing prices.

In the short-term further restrictions on loan to values may be used until the Reserve Bank has time to undertake full consultation on DTI'S and an impact assessment completed. The Reserve Bank has stated this does not mean that these debt-to-income ratios will be implemented. However, groundwork will be completed now in the anticipation it will be required and the uncertainty, with all its detrimental side effects, remains for property investors and developers.

Sharon Cullwick
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