

More lenders offer escape route from 'mortgage prison'

Borrowers stuck in expensive loans are finding a way out thanks to fierce competition among providers.

Duncan Hughes *Reporter*



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Resimac Group, a leading non-bank lender, and Westpac are offering borrowers an early release from “mortgage prison [<https://www.afr.com/policy/economy/16pc-of-households-locked-in-mortgage-prison-rba-20230406-p5cypj>]” by slashing serviceability buffers, making it easier for borrowers to refinance and triggering a fierce response from rivals.

Mortgage brokers claim buyers are playing off competing lenders to refinance from loans they would otherwise be trapped in due to not owning adequate capital in their homes.



Borrowers seeking a cheaper loan will need to prove that they have an exemplary repayment record and can comfortably service the new loan, say brokers. **Simon Letch**

Resimac and Westpac have eased the three percentage point servicing buffer set by the Australian Prudential Regulation Authority (APRA). Resimac has lowered this to two percentage points, while Westpac is believed to have gone lower.

Scott McWilliam, CEO of Resimac Group, says: “Following a comprehensive analysis of the interest rate outlook, we felt that a reduction in the serviceability assessment buffer was the right decision. We’re confident that a 2 percentage point buffer still provides sufficient headroom should rates rise in the short term, and it gives customers a greater opportunity of entering the property market, refinancing their loan or using debt consolidation to assist with managing their commitments.”

Under the APRA stress test, every new home loan applicant must show they can afford monthly repayments at three percentage points more than they are applying for, or the bank’s pre-set floor rate (whichever is higher). A floor rate is the minimum rate a borrower will be charged.

“You’re not trapped, we’ll take you’, lenders are telling borrowers,” says Phoebe Blamey, a director of mortgage broker Clover Financial Solutions.

Matt Turner, managing director of GSC Finance Solutions, adds: “We are getting trapped borrowers out of mortgage jail by leveraging off lenders’ new servicing policies.”

Chris Foster-Ramsay, principal of Foster Ramsay Finance, says: “If some lenders have moved to easing loan servicing, then others are likely to follow.”

“If they are not relaxing their lending criteria, then they are more amenable to discounts. Lenders are aggressively competing for new business.”

The Westpac changes also apply to subsidiaries St George, Bank of Melbourne and BankSA.

Mortgage brokers say other lenders are easing conditions for borrowers [<https://www.afr.com/link/follow-20180101-p5d93i>] with impeccable repayment histories and steady incomes, despite the possibility of more rate rises.

“But they are moving more discreetly than lenders that have cut serviceability buffers by negotiating on a loan-by-loan basis,” says Turner.

Lenders typically stress test borrowers’ finances to ensure they can afford mortgage repayments if rates rise by three percentage points above the loan they are applying for.

This has stopped some borrowers from being able to refinance to a cheaper loan, effectively locking them into their borrower.

Potential savings from refinancing*

	Rate (%)	Monthly repayments (\$)	Cost over next 2 years (\$)
Current	6.44	6,190	125,270
After refinancing	5.59	5,675	106,266
Difference	-0.85	-515	-19,004

*Based on an owner-occupier taking out a \$1m loan 2 years ago.
Source: Ratecity

For example, according to National Australia Bank one in five of its home loan customers are “mortgage prisoners” who cannot switch banks because higher interest rates prevent them from clearing serviceability buffers at a new lender.

Hardest hit are likely to be first home buyers who bought at the peak of the market with a small deposit.

The number at NAB is two in five for those who borrowed between August 2019 and July last year, when rates were at their lowest.

Borrowers seeking a cheaper loan will need to prove that they have an exemplary repayment record and can comfortably service the new loan, say brokers.

Interest-only loans, debt consolidation and loans that require lenders' mortgage insurance typically will not qualify. Also excluded are applications that include a guarantor, which would bar most bank of mum and dad applicants

[<https://www.afr.com/wealth/personal-finance/bank-of-mum-and-dad-in-trouble-as-young-borrowers-struggle-20221011-p5bovh>].

Borrowers applying for Westpac’s “streamlined refinance” must have not fallen behind in repayments or reported hardship during the past 12 months. The loan to value ratio must be below 80 per cent and new loans must be principal and interest.

The borrower will be asked to declare there are no foreseeable material or adverse changes to their ability to repay the loan.

APRA, which sets lending standards, does not prevent banks from approving mortgages outside standard criteria, even though 97 per cent of loans meet the regulator’s standards. The rules do not apply to non-bank lenders.

Critics [<https://www.afr.com/policy/economy/call-to-scrap-credit-test-to-free-households-from-mortgage-prison-20230519-p5d9nq>] of the APRA stress test argue that while the three percentage point buffer helps ensure new borrowers do not take out excessive debt, it also prevents others from being able to move to a cheaper lender.

“These are often households that borrowed at or near capacity when rates were at record lows and the APRA stress test was 2.5 per cent,” says Sally Tindall, research director at RateCity, which monitors lending rates.

Since then, buffers have been raised to three percentage points and the Reserve Bank of Australia has increased the cash rate from 0.10 per cent to 3.85 per cent.

“Yet it is these borrowers who are likely to need rate relief more than ever to help stay afloat,” says Tindall.

Bank chiefs, including NAB chief executive Ross McEwan, say the potential for higher interest rates to reduce mortgage competition could force regulators to reassess the level of serviceability buffers,

CBA, the nation’s largest lender, says customers seeking refinancing or new lending will be assessed in line with regulatory requirements and it will “not apply any differentiated buffer”.

The accompanying tables show potential home loan stress test rates under different serviceability buffers, and potential savings from moving to a cheaper lender.

Stress test rate under different serviceability buffers		
	Big 4 basic variable rates* (5.97%)	One of lowest variable rates (5.25%)
Current buffer 3% pts	8.97	8.25
If buffer was 2% pts	7.97	7.25
If buffer was 1.5% pts	7.47	6.75
If buffer was 1% pts	6.97	6.25
*Average of each bank's ongoing variable rate with a 20% deposit. Source: Ratecity		

For example, an owner-occupier borrower with a \$1 million loan who reduces their loan by 0.85 percentage points to 5.59 per cent would save around \$19,000 in repayments over the next two years.



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