

Loan-to-Value Ratio Restrictions on Residential Property

As of 1 October 2013 all banks in New Zealand are required to restrict new residential mortgage lending at a loan-to-value ratio ("LVR") of over 80 percent to no more than 10 percent of the value of the bank's residential mortgage portfolio.

The LVR is a measure of how much a bank lends against a residential property, compared to the value of that property. To calculate your potential LVR to see if you may be considered as having a high LVR you can divide your desired loan value by the valuation of the property you intend on purchasing. For instance, a property with the value of \$400,000.00 would require a deposit of at least \$80,000.00. Any less than \$80,000.00 would result in a LVR above 80 percent, be deemed a high LVR loan and caught by the restrictions.

The LVR restrictions have been introduced by the Reserve Bank whose role is to promote a sound, stable and efficient financial system. Over the last several years, the Reserve Bank has become concerned about the rate at which house prices have been increasing (especially in Auckland and Christchurch) and has been considering a range of different options to potentially address this.

The Reserve Bank believes that the implementation of the LVR restrictions is the best option to help slow the rate of housing-related credit growth and house price inflation. This in turn should reduce the risk of a significant fall in house prices at some point in the future which is seen by the Reserve Bank to be a "real threat" and one which would be greatly damaging to the financial sector and the broader economy in New Zealand.

Note that this is not an entire prohibition of lending on residential properties with a LVR of 80 percent or higher. If your available funds for a deposit are less than 20% it will be up to your bank to decide whether it is prepared to lend money to you. However one bank, ASB, took the action of withdrawing its loan pre-approvals for borrowers with less than 20 percent equity.

Although banks can use their discretion (within their 10 percent limit), the LVR lending rules are still considered by most to be a significant restriction and an additional hurdle especially for first home buyers looking to get on the property ladder.

At this stage there are several areas where the Reserve Bank has indicated further rules are to be announced within the next few months to ensure that the new regime and policy is not undermined. For instance, although initially each bank is able to rely on its own policy on the determination of a house's value, the Reserve Bank has said that it is looking at tightening the rules in this regard by requiring independent property valuations. Potential borrowers should also be aware that down the track the Reserve Bank may require that credit cards and personal loans be included in the calculation of the loan value to prevent a borrower using that lending as part of their deposit, thereby avoiding the LVR restrictions. For the time being however each bank will have its own policy on the calculations of the loan value.

If you would like more information on the LVR restrictions, or how they may affect you (especially if you have home loan pre-approval from your bank), please contact one of our specialist property team.

Further information on the LVR restrictions can also be obtained on the Reserve Bank website: www.rbnz.govt.nz.