



Mr Wayne Byres
Chairman

Australian Prudential Regulation Authority

Developments in housing markets

Wednesday 11 July 2018 - Sydney



APRA

Preparing for a rainy day

Australian Business Economists Lunchtime Briefing
11 July 2018

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Chairman
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A sound banking system



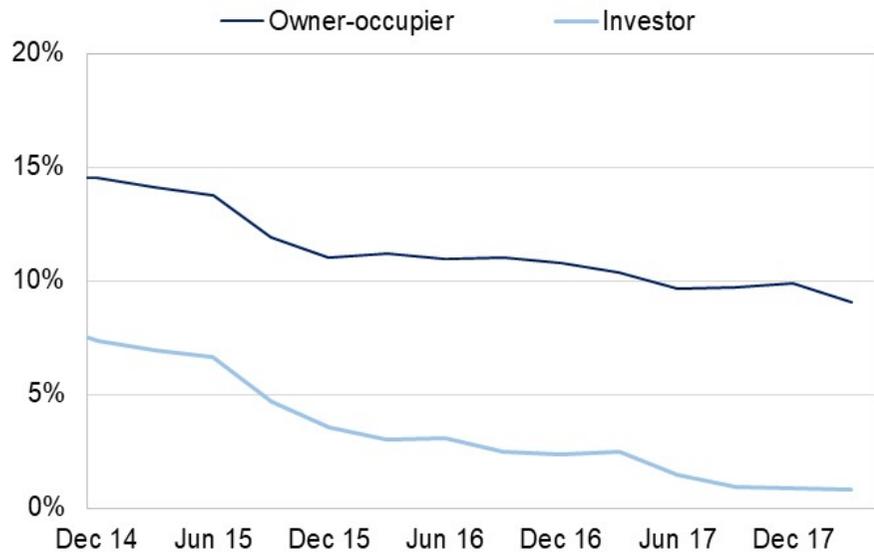
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- Australian banking system financially sound
- But so it should be after a long period of economic expansion
- Good times don't last forever, so a prudent strategy for banking is to:
 - maintain sound lending standards when sun is shining and winds are calm;
 - building financial resilience today to protect against stormy weather in the future; and
 - preparing contingency plans to ride out a severe storm, if one does hit

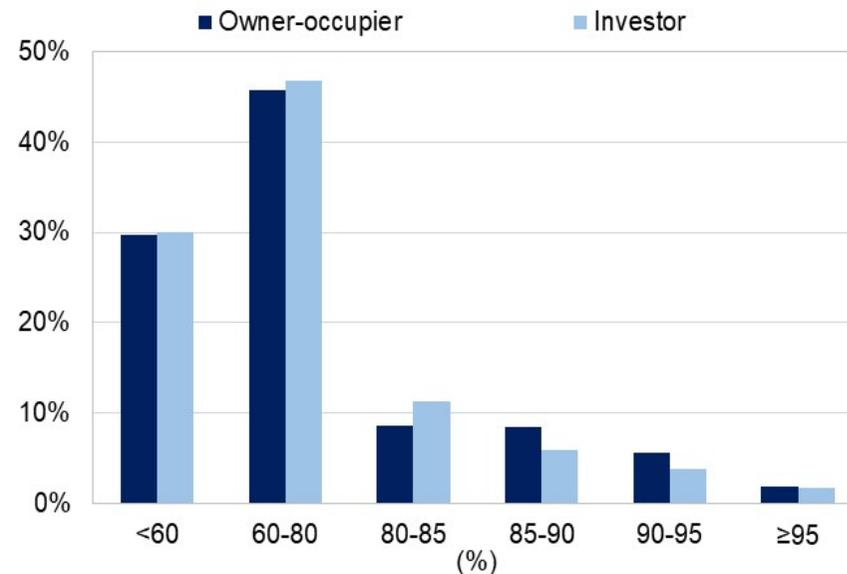
While the sun shines – maintain sound standards



**LVR ≥ 90 per cent
(share of new lending)**



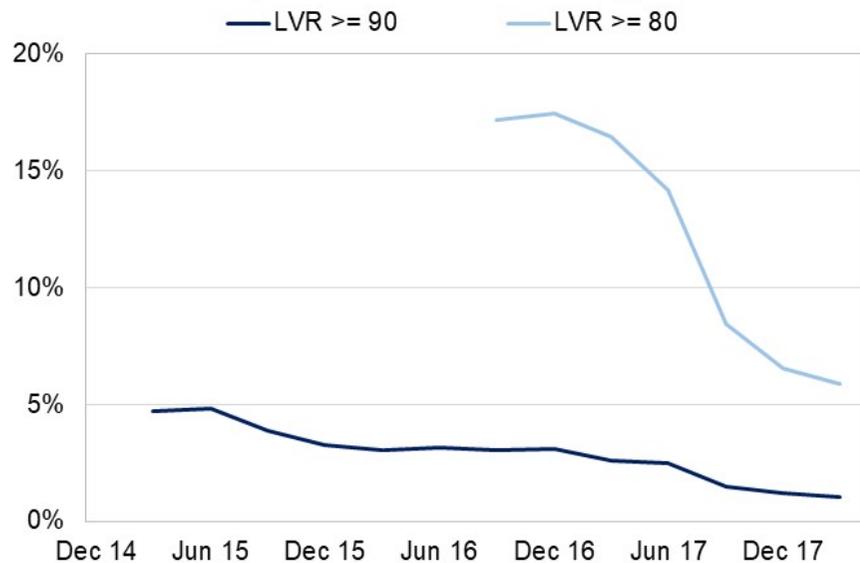
**Residential mortgage term loans outstanding
by LVR, Mar 18**



While the sun shines – maintain sound standards



High LVR and interest only lending (share of total new lending)



Interest only lending with term > 5 years (share of total new lending)

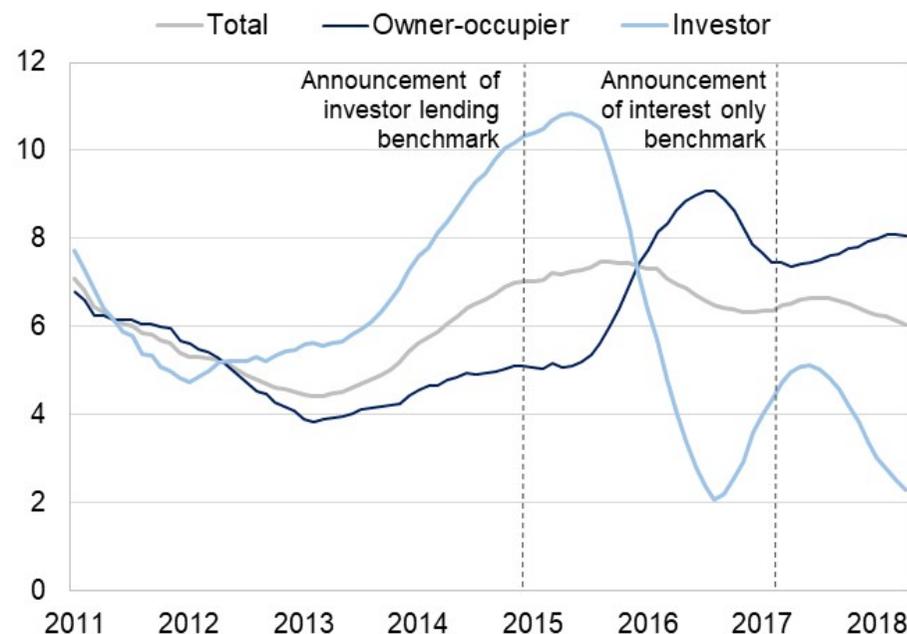


Reinforcement of lending standards



- Improved portfolio metrics correspond with strengthened credit assessments
- Lifting industry standards neither quick nor straightforward
- Heavy lifting largely done; announced lifting of investor growth benchmark
- Impact on flow of credit:
 - difficult to disentangle impacts
 - aggregate housing credit growth – little obvious impact
 - composition of housing credit – major shifts
- Lending to owner occupiers has grown strongly despite tighter standards

Housing credit growth (% per annum)



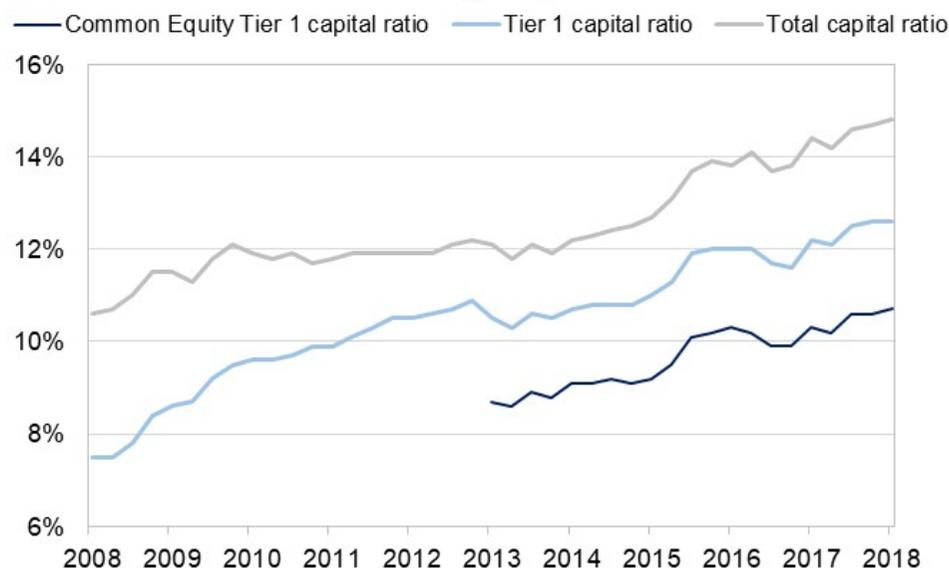
When a storm hits – testing resilience



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- Decade long build up in capital almost complete
- Available to absorb losses in downturn
- Stress testing assesses adequacy of defences to a period of stormy weather

ADI industry capital ratios

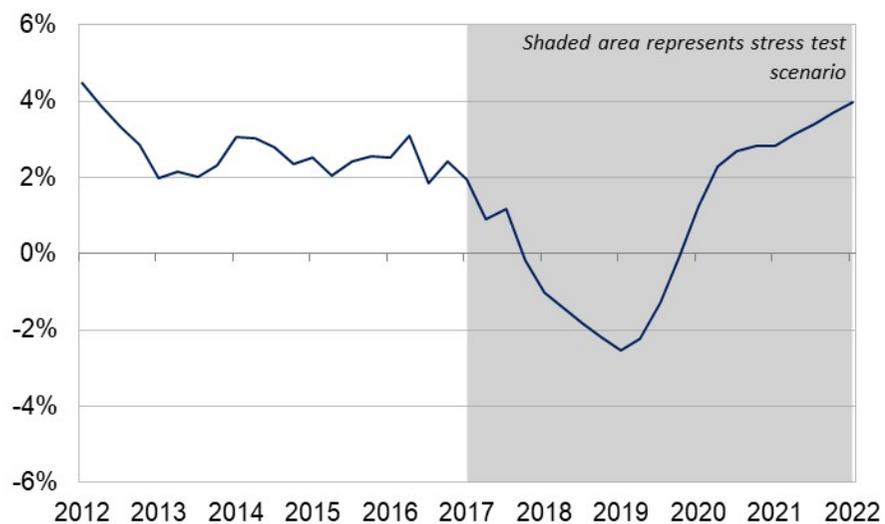


Capital data presented is collected under different APRA reporting frameworks: the Basel II capital framework from 1 January 2008, and the Basel III capital framework from 1 January 2013.

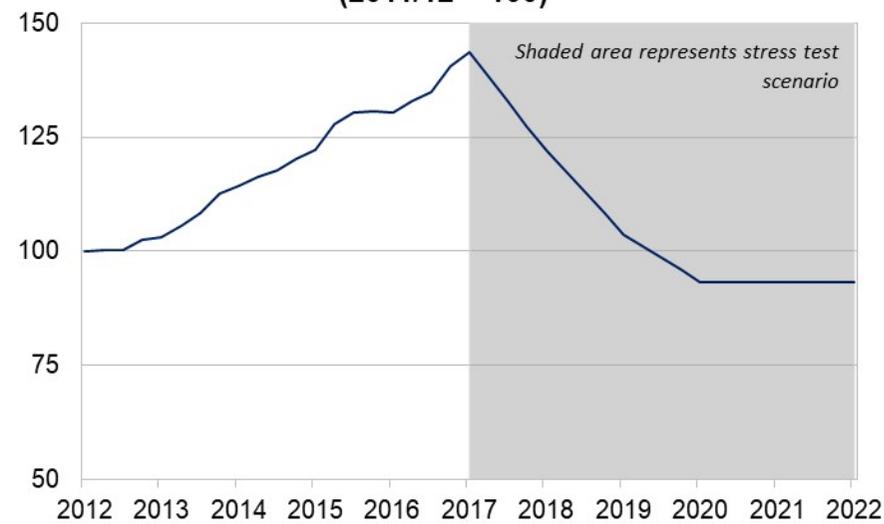
When a storm hits – stress testing



Stress test - Real GDP growth



Stress test - House price index (2011/12 = 100)

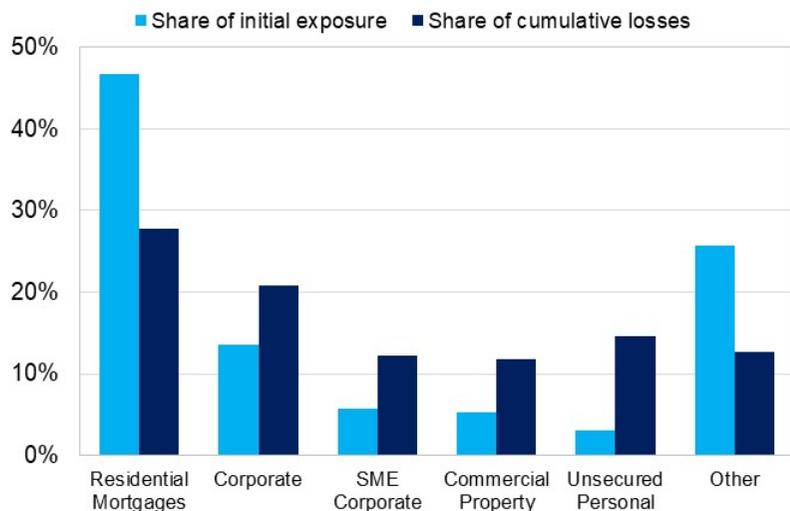


When a storm hits – stress testing

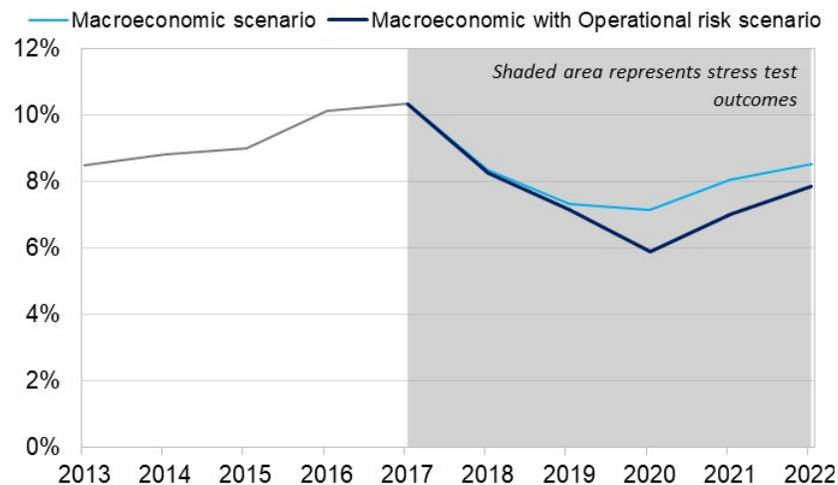


- As expected, scenario generates significant losses across industry, including on mortgage portfolio
- CET1 capital ratio down by close to 3.5 p.p. in macro scenario; additional 1 p.p. from op risk

Proportion of cumulative credit losses



**CET1 capital ratio results
Macroeconomic and operational risk scenario**



The aftermath – recovery planning



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- Resilience means banks not only survive a scenario but can keep lending
- Recovery plans provide options to rebuild after balance sheet damage
- Pre-thinking and positioning for:
 - capital raisings;
 - portfolio restructuring;
 - repricing and cost cutting; and/or
 - asset sales and business disposals.
- Important to have plans that are credible, realistic, operational, and with sound governance and triggers for action

Concluding remarks



- It has been a long time since a serious economic storm hit the Australian banking system
- But it will happen some day, so building resilience in good times is essential
- APRA's actions therefore multi-dimensional:
 - reinforce lending standards
 - build capital to absorb future losses
 - regularly assess stressful scenarios
 - keep recovery plans in focus
- No guarantees against stormy weather, but better prepared to deal with it



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Dr Philip Lowe
Governor
Reserve Bank of Australia

Demographics and recent developments in monetary policy

Wednesday 08 August 2018 - The Westin Sydney
The Anika Foundation

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