Trends and drivers of high-LVR lending

An AFR article attributed a declining trend in high-LVR lending to worsening affordability and increased participation of higher income purchasers with large deposits. While some of the decline in high LVR lending can be attributed to affordability pressures, there are other dynamics at play.

Our analysis identifies that the declining LVR trend and drivers can be bifurcated into two phases over the past three years. **Falling FHB participation and savings buffers** built during COVID were the major contributors to the initial decline in high-LVR lending from early 2021 to mid-2022. **Growing refinancing activity** was the main driver of the trend between mid-2022 and late 2023. The share of high-LVR lending has increased more recently as refinancing activity decreased.

Observed trends:

- **High-LVR lending (LVR ⩾ 80) fell sharply between December 2020 and September 2023**. The decline was driven by owner-occupied housing loans, with their high-LVR lending share falling from 46 per cent in December 2020 to 28 per cent in Sep 2023 (Chart 1). This trend reversed in December 2023.

- **The size of new loans increased, but at a lower rate than property prices**. The average new loan commitment increased by 21 per cent between December 2020 and December 2023 (excluding refinancing), compared to the 28 per cent increase in the Hedonic Home Value over the same period.

Key drivers:

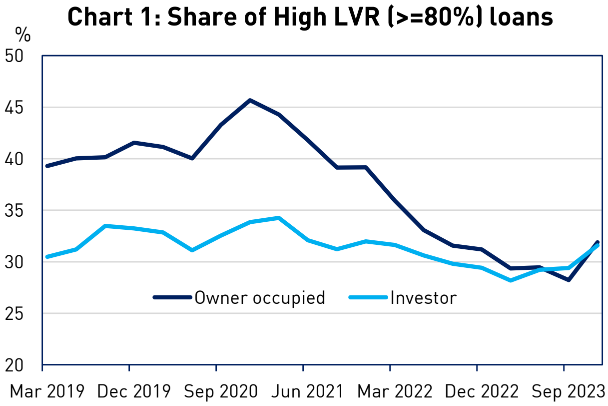
- **Lending to FHBs decreased after peaking in December 2020** (Chart 2). FHBs typically borrow at higher LVRs as they tend to have limited savings – 70 per cent of FHBs borrowed with a high LVR in 2023 (chart 3). FHB activity accelerated during the pandemic, peaking at December-20, encouraged by low interest rates. Affordability pressures from rising interest rates over the past two years and increasing house prices have led to a decline in FHB activity and in the overall level of high-LVR lending. Current FHB activity levels are consistent with historical norms.

- **High savings buffers built during COVID** helped purchasers with their deposit during the pandemic, reducing LVRs at margin. COVID led to an increase in savings across most income levels (Chart 4), driven by government support and lower consumption opportunities.

- **Refinancing activity was at an all-time high** (Chart 5). Refinanced loans typically have lower LVRs, as the accumulated equity of the borrower is recognised in the loan assessment. External refinancing activity accelerated from around mid-2022 in line with increased competition (i.e. cashbacks) for market share, lowering the relative share of high LVR lending at an aggregate level. Excluding refinancing, the high LVR share of new lending was relatively flat over (Chart 6). Refinancing activity has since reduced, and the share of high-LVR lending has increased.

Charts

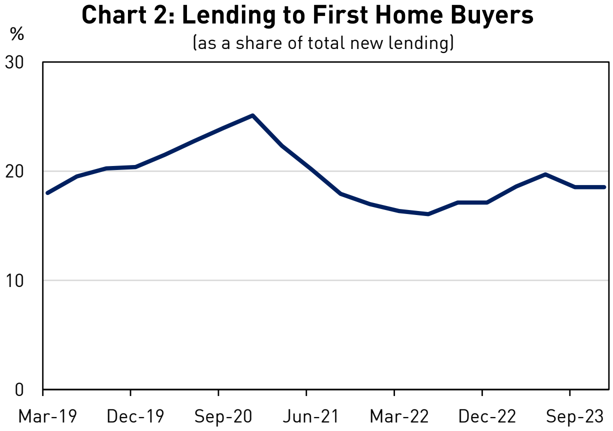
Chart 1: Share of High LVR (>=80%) loans



Source: ARF 744.0

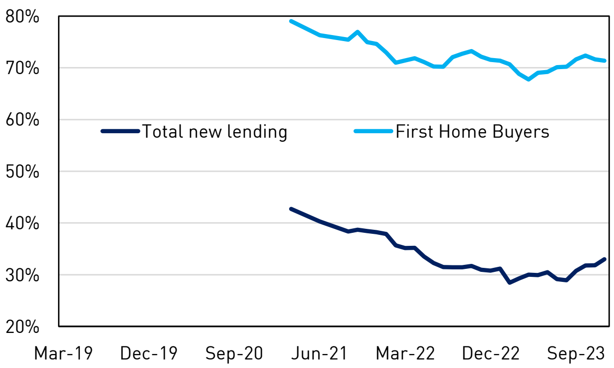
Chart 2: Lending to First Home Buyers

(as a share of total new lending)



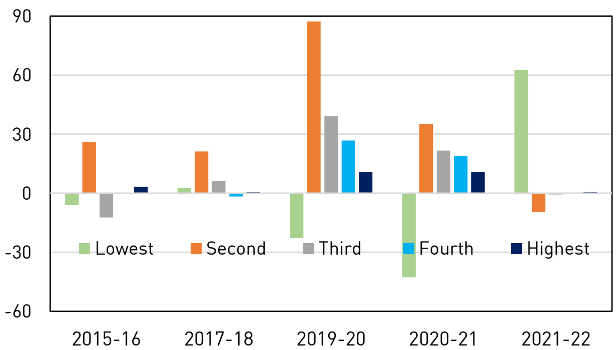
Source: ABS, Seasonally adjusted, ADIs and Non-ADI Lenders

Chart 3: Share of high LVR (>=80) loans



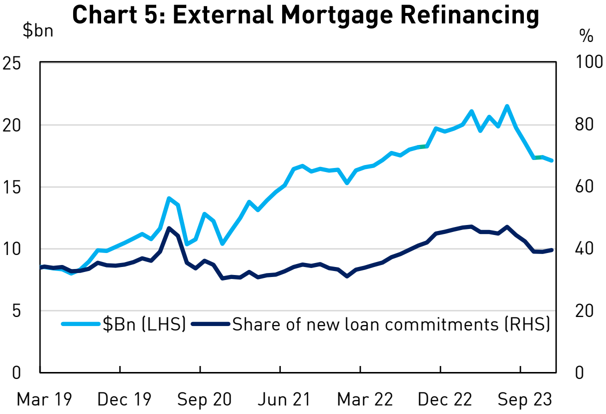
Source: ARF 923.5, best endeavour collection

Chart 4: Annual increase (%) in gross saving by income quintiles



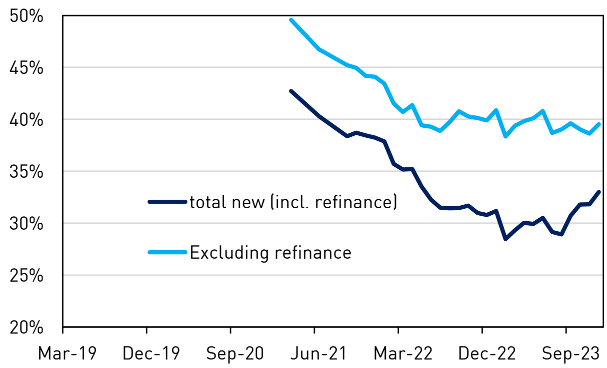
Source: ABS

Chart 5: External Mortgage Refinancing



Source: ABS, Seasonally adjusted, ADIs and Non-ADI Lenders

Chart 6: Share of high LVR (≥80) loans



Source: ARF 923.5, best endeavour collection