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ARTICLE

The global financial crisis and the Australian and New Zealand housing markets

Laurence Murphy

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Abstract The evolution of the US sub-prime mortgage meltdown into a global financial crisis clearly demonstrates the increasingly integrated nature of mortgage and capital markets. However, notwithstanding the global scale and severity of the recent financial crisis, the effects of the credit crunch were mediated by nationally constituted housing markets, the activities of local financial institutions and national housing policies. Adopting an institutional perspective this paper critically examines the manner in which the financial crisis impacted upon the Australian and New Zealand housing markets. These countries had actively participated in the liberalisation of mortgage markets and experienced significant house price inflation post-2000 but, in contrast to the USA and some European experiences, they escaped a severe housing downturn. It is argued that a combination of pre-existing institutional practices, market conditions and government policies acted to shelter these markets and created the potential conditions for a new housing boom. While avoiding a deep housing slump, both Australia and New Zealand have to address the on-going macroeconomic implications of a system predicated on housing inflation and capital gains.

Keywords Global financial crisis · Australia and New Zealand · Mortgage liberalisation · Mortgage institutions

1 Introduction

The role of the US sub-prime mortgage meltdown in triggering the global financial crisis (GFC) highlights the manner in which housing finance systems have evolved over the last 40 years. From relatively discrete and sheltered finance systems, mortgage markets have increasingly become part of a globalised financial architecture embedded in international capital markets (Green and Wachter 2010). Since the 1980s economic globalisation,

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financial deregulation, securitisation and processes of disintermediation have reshaped the institutional structures and agents that channel money into mortgage markets around the world. The depth and severity of the recent global financial crisis has had profound implications for national economies, mortgage markets and housing markets (IMF 2008; OECD 2009a, b; Smith and Searle 2010).

During the post-2000 global residential property boom considerable attention was given to the role of finance capital and economic growth in propelling house prices. The highly synchronised nature of national residential property booms across the globe, promoted by a global decline in inflation and interest rates, helped to shape an economic rhetoric that had the effect of homogenising the performance of housing markets (Ball 2010). However, while financial liberalisation had reshaped mortgage markets and promoted the globalisation of funding, the nature of change and the practices of institutions varied internationally. In the context of the post-2007 global credit crisis, and the unfolding media and economic discourses on economic change, it is important to recognise that differing banking structures and agents, in conjunction with differences in national housing and mortgage markets, have shaped the manner in which national housing markets have been affected by the crisis. Indeed, the sub-prime mortgage crisis itself was the product of a set of processes associated with specific institutional actors and practices operating within a specific housing market.

This paper examines issues affecting the Australian and the New Zealand housing markets in the wake of the financial turmoil. The paper considers the pre-existing institutional context in which the global crisis played out in these countries and outlines the various government and regulatory responses that emerged. While both countries were clearly participants in the post-2000 global housing boom and underwent considerable financial liberalisation, their housing market dynamics differ from the USA and European experiences and, despite the shared financial sector linkages, differ from each other. Both countries have traditionally had high levels of home ownership that reflect persistent policy support for the tenure. Significantly, the banking authorities in both countries had, prior to the crisis, sought to combat house price inflation through increasing interest rates (Berry 2010; Murphy 2009). At that time the monetary authorities were concerned with the overwhelmingly dominant position of housing assets in household wealth formation and the problem of declining housing affordability. Yet in reacting to the post-2007 financial crisis it is arguable that the resultant policy responses have acted to reinforce the role of home ownership as an asset and are creating the conditions for further property booms. Moreover, the primacy of home ownership as a tenure in these countries, and the role of housing in wealth formation, means that government policy is increasingly bound to support house price growth, even if this is inherently problematic.

The remainder of the paper is in six parts. First, I review issues relating to the changing dynamics of mortgage markets and the role of the US sub-prime mortgage market in precipitating the global financial crisis. This section locates the current analysis within a wider institutional literature. Having argued that institutions matter, the next section of the paper provides details on the structural characteristics of the Australian and New Zealand mortgage markets, focusing on mortgage agents and products. Next I provide an overview of developments in the Australian and New Zealand housing markets prior to the credit crunch, paying particular attention to the manner in which mortgage markets evolved. In the next two sections I critically examine the Australian and New Zealand policy responses to the global financial crisis that were introduced to address problems in the respective housing markets. The concluding section reflects on the distinct experiences of the Australian and New Zealand housing markets and comments on the continued significance and problems of home ownership in these countries.

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2 The dynamics of mortgage finance and housing markets

The transformation of the US sub-prime mortgage crisis into a global financial crisis offers a prime example of how globalisation works to intensify the local/global dialect. The origination of sub-prime mortgages is essentially a set of individual (generally modest scale) property transactions embedded in very local housing markets (Crump et al. 2008; Foote et al. 2008; Wyly et al. 2006, 2008). Through securitisation and other forms of structured finance, individual mortgage payments are bundled together and distributed across the global financial system (Green and Wachter 2010). In the boom, the globalised nature of certain elements of the finance system ensured the flow of funds that fuelled the system. In the crisis, the financial problems of individual households, in specific local housing markets (Immergluck 2009; Schuetz et al. 2008), undermined sophisticated funding structures and the resultant problems were transmitted into a global crisis of confidence in the financial system (Green 2008; Sanders 2008; Smith and Searle 2010).

The nature and consequences of the US sub-prime crisis highlight both the benefits and problems of financial globalisation. In addition, the US housing crisis challenged an emerging policy consensus regarding the perceived benefits of home ownership and in particular the belief that home ownership was a relatively 'riskless' investment. Significantly, the US sub-prime crisis clearly demonstrated how specific financial institutions and practices combined with government policy helped shape market structures and outcomes. As home ownership was increasingly promoted as a tenure in the USA, the regulatory constraints on mortgage origination practices lapsed, since markets were believed to have developed the capacity to price risk appropriately. The pressure to generate turnover in a booming market resulted in mortgage origination practices that are now deemed predatory (Wyly et al. 2008; Wyly 2010). During the boom, asymmetric information flows helped to underpin the growth of the sub-prime market and its increasing securitisation (Green 2008). International investors who were not attuned to the institutional differences between prime residential mortgage-backed securities (RMBS) offered by government-sponsored enterprises (GSEs) and sub-prime private label (usually Wall Street banks) RMBS were rapidly educated in their differences (Green 2008; Sanders 2008). However, as the crisis unfolded even these distinctions were lost, as investors shunned different forms of securitisation and a crisis of confidence in the banking sector resulted in a global credit crunch.

The broad lineaments of the USA housing boom (rapid price appreciation, liberal finance markets, low interest rates etc.) were shared by a host of other economies including the UK, Spain, Ireland, the Netherlands, Australia and New Zealand. On the basis of simple (and problematic) house prices to rent ratios, housing markets around the world were viewed as being excessively overvalued for some time (The Economist 2003). Thus in the face of the sudden reversal of the US housing market post-2007, there were legitimate fears of a global housing market crash. As the global financial crisis intensified throughout 2008, there were dramatic falls in house prices across the globe (OECD 2009b). In particular housing markets associated with advanced mortgage systems were seen to be vulnerable to considerable price corrections (IMF 2008). Yet, notwithstanding the macroeconomic similarities in the experiences of different housing markets, national housing markets remain structurally differentiated. Thus the effects of the global financial crisis were mediated by nationally constituted structures of housing provision (Ball 2006, 2010).

The spatially uneven impacts of the global financial crisis on national housing markets highlights the importance of understanding the institutional character of housing systems. With respect to Europe, Albers (2009a) argues that processes of globalisation and Europeanisation did not promote a deterritorialisation of mortgage markets. He argues that while

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secondary mortgage markets were increasingly globalised, "most primary mortgage markets remain(ed) largely national" (p. 389) in nature. For Albers (2009a) the existence of nationally constituted taxation, cultural and legal systems, combined with the limited role of foreign mortgage intermediaries in national markets, restricted deterritorialisation processes. Developing upon this thesis it can be argued that since mortgage markets are the products of institutional processes, and are shaped by the operations of mortgage agents and state institutions (Albers 2009b), an understanding of the character and evolution of institutional practices and arrangements is essential in analysing the impacts of global shocks.

Within housing studies there is a long tradition of research from an institutional perspective (Ball 1986, 2003, 2006, 2010; Burke and Hulse 2010). Ball (2010) observes that the pessimistic prognosis of market commentators during the crisis, predicting a 'sharp correction' of global house prices, did not materialise and the actual reaction of economies and real estate markets varied widely. Consequently, he maintains that the "maxim of the importance of spatial differences … once again was proved relevant within and across countries" (p. 932). Ball (2010) shows how the 'long European housing boom up to 2007' (p. 935) was marked by significant variation in market dynamics across countries. For example, the relationship between rising mortgage debt and house price increases was particularly strong in countries such as "Denmark, Ireland, Netherlands, Spain and the UK" but was less significant in countries such as Belgium and France, where prices rose but mortgage debt to GDP ratios remained low (p. 935). In addition, the supply responses to house price increases varied significantly. Both Ireland and Spain experienced considerable housebuilding booms whereas the Netherlands and the UK did not. He argues that while global forces such as the "general easing in credit, declining inflation … real interest rate declines" (p. 936) shaped the boom in prices, local factors relating to economic performance, demographics, "housing policy and local supply-side issues" were also significant. These institutional, demographic and economic factors not only shaped the boom but also the response to the crisis.

Drawing on the literature that emphasises institutional frameworks, and recent analyses that have examined the impact of the global crisis on national real estate markets (Albers 2009a, b; Ball 2010; Burke and Hulse 2010; Pollard 2010), this paper uses secondary data and a critical analysis of policy documents to examine the institutional and policy contexts in which the Australian and New Zealand housing markets have evolved and responded to the global crisis. By focusing explicitly on the experiences of Australia and New Zealand the paper contributes to alternative accounts of the crisis that differ from the dominant narrative of housing crisis emanating from the US and UK experiences. Moreover, by focusing on Australia and New Zealand the paper demonstrates how countries that share a history of promoting home ownership and embraced mortgage market liberalisation experienced divergent outcomes.

3 The institutional character of the Australian and New Zealand mortgage markets

The institutional structures associated with the production, consumption, exchange and management of housing are nationally constituted (Ball 1986) and have significant implications for the nature and operation of housing markets (Ball 2003; Burke and Hulse 2010). While the Australian and New Zealand housing markets share similar structural characteristics compared to other countries with high levels of home ownership, they also have distinct institutional structures. Home ownership as a tenure in Australia and

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New Zealand is strongly aligned with the market dominance of single detached houses located on their own block of land (Burke and Hulse 2010; Murphy 2009). In contrast to the UK, but similar to the USA, housing production involves a land development industry and a building industry. Significantly, Burke and Hulse (2010) argue that production is centred on a 'contract method' rather than speculative development model. This contract method involves the conversion of land into individual sites and the construction of houses by individual builders contracted by individual consumers. This model ensures that "there is little speculative construction" (Burke and Hulse 2010, p. 827) and in a downturn it reduces the potential for overproduction based on speculative development. Moreover, the ways in which house purchases are financed also have a significant bearing on the evolution of a housing market. Given the focus of this article, the distinguishing characteristics of the Australian and New Zealand mortgage markets need to be set out in detail in order to contextualise the remainder of the argument.

The general character and evolution of the Australian and New Zealand mortgage markets aligns more closely with the UK mortgage system than the US system. Traditionally, retail (deposit-taking) banks have been the dominant mortgage originators that supplied a limited range of mortgage products within a highly constrained credit rationing system. The most common mortgage instrument was the variable-rate mortgage, where the rate is "set by the lender at its discretion (a reviewable-rate loan)" and "the rates on these loans are changed for all borrowers at the same time" (Lea 2010, p. 18). The dominance of adjustable- or variable-rate mortgages offers significant benefits for the banks by allowing them to align the rates offered to depositors (the cost of funding) with the rates set for borrowers and thus minimising interest rate risk (Lea 2010). In contrast to the US, where fixed-rate mortgages have traditionally dominated and where adjustable-rate mortgages have been viewed as a source of instability, the variable-rate mortgage system in Australia and New Zealand has proved to be relatively robust. In addition, and in contrast to the US, mortgages remain on the balance sheets of the banks and securitisation has been limited, until recently.

Traditionally, lenders have employed conservative lending standards that have required borrowers to contribute a substantial deposit, provide documentation of income and demonstrate a capacity to repay the loan. In Australia the regulatory authorities place significant obligations on lenders to implement responsible lending programmes. Mortgages in Australia and New Zealand are 'full recourse' and allow lenders to "pursue deficiency judgements" (Lea 2010, p. 32), that require borrowers to repay the full value of the loan when in default, even if they are in negative equity (i.e. when the value of the loan is greater than the value of the house). Consequently, these markets have been characterised by low levels of mortgage default.

Since the 1980s both the Australian and New Zealand mortgage markets have been liberalised, resulting in new players entering the market and the introduction of new mortgage products. Despite the fact that all of the major retail banks in New Zealand are Australian owned, the markets have diverged in several ways. In Australia during the 1990s new wholesale-funded mortgage originators entered the market. These originators tapped the wholesale money markets to fund their operations and securitised their mortgage books. This was a popular strategy for institutions that had limited access to retail deposits via branch networks. At their peak these institutions accounted for 15% of new mortgage approvals. In addition, mortgage brokers entered the market, channelling borrowers to the new originators and promoting intense downward pressure on the banks' mortgage margins by encouraging borrowers to 'shop around'. New mortgage products have been introduced including conversion mortgages (variable to fixed), flexible mortgages, and multiple

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fixed- and variable-rate mortgages on the same property. While new products were introduced sub-prime mortgages remained a small part of the Australian mortgage market and exotic mortgages (such as negative amortisation) were not introduced.

In broad terms the New Zealand mortgage market followed the Australian market in terms of product innovation, the rising importance of mortgage brokers and increased competition. However the markets differed in two key respects. First, in New Zealand the four major retail banks dominated the market and wholesale-funded mortgage originators did not enter the market. Second, fixed-rate mortgages of 1–5 years duration came to dominate and accounted for over 80% of the market. This unusual situation reflected the specific contingencies of the New Zealand economy. As the Reserve Bank of New Zealand (RBNZ) sought to reduce inflation pressures it raised short-term lending rates by increasing the official cash rate (OCR). This raised variable mortgage rates but also created the opportunity for the banks to access cheaper wholesale funds and offer fixed-rate mortgage rates below the variable rate. The availability of relatively 'cheap' fixed-rate mortgages helped to sustain a house price boom from 2002 onwards (House Prices Unit 2008).

4 Before the storm: overview of the Australian and New Zealand housing markets

Australia and New Zealand have long histories of housing policy regimes that have favoured the expansion of home ownership. Within the context of the evolution of a 'wage earners welfare state', Castles (1996, p. 94) argues that, "by the 1950s and 1960s governments in Australia and New Zealand were treating home ownership as a welfare good to be provided for all classes of the population through subsidized or interest-regulated loans". Under the aegis of different governments, home ownership levels have been consistently high and are currently at approximately 70% in Australia and 66% in New Zealand (ABS 2008; Thorns 2009). Within the public and political discourses that have shaped these settler nations, and have sustained the image of Australia as the 'Lucky Country' and New Zealand as 'Godzone' (God's own), is the perception that home ownership is a rite of passage for most, if not all, citizens. The suburban 'quarter-acre' dream carries significant ideological force in these countries and political parties of various hues are strongly supportive of this tenure, which is seen to encourage self-reliance and good citizenship (Murphy 2009).

While home ownership has long been a dominant tenure in these countries, the character and experience of home ownership has evolved over time as the institutions and agents involved in the provision of this tenure have changed (Ball 2006). In particular, the Australian and New Zealand governments' engagement with neo-liberalism prompted a significant liberalisation of finance markets and altered the nature of housing finance. The role of the state as a supplier of mortgage finance declined and the banks became the main source of mortgage funding (Murphy 2000). In line with international trends in housing finance systems, the Australian and New Zealand mortgage markets shifted from credit constrained and conservative lending regimes to more price competitive and product innovative markets (Berry 2010; Green and Wachter 2010; Murphy 2009). Indeed the IMF described Australia, with the United States, Denmark, Sweden and the Netherlands, as having "the most flexible and "complete" mortgage markets" (IMF 2008, p. 106).

The combination of economic growth and more liberalised mortgage markets (that assisted housing equity withdrawal and increasingly linked household consumption with house price appreciation) facilitated Australia and New Zealand's participation in the

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post-2000 global property boom. Figure 1 provides data on house prices in Australia, New Zealand, the US and the UK. Australian house prices accelerated rapidly from 2000 to 2004, promoting an affordability crisis. In response to negative inflationary aspects of the property boom, the Reserve Bank of Australia raised interest rates and house price increases slowed down thereafter. Significantly this downturn in the market predated the GFC by several years and meant that the Australian banking system had already adjusted to a slowing market in advance of the global crisis. In contrast, New Zealand's boom saw house prices increase by 80% in real terms between 2002 and 2007 (House Prices Unit 2008) and house prices were increasing right up to the global crisis. In nominal terms New Zealand's house price appreciation was comparable to the UK and US experiences.

In Australia, a mixture of short-term (declining interest rates, increasing investor demand), institutional (financial deregulation) and long-term (demographic changes, economic growth) factors precipitated rapid house price inflation and problems of housing affordability in the post-2000 period (Berry and Dalton 2004). Between 2000 and 2006 real house prices increased at an annual average rate of 7.1% (OECD 2009b). In July 2000 the Australian government introduced a first home owner grant (FHOG) of A$7,000 in order to "offset the net price effect from ... indirect tax changes" (Wood et al. 2006). While providing assistance to first-time buyers, the scale of the housing boom meant that affordability problems persisted. Yates (2008) is particularly critical of the effectiveness of such support in the long run.

Underpinning the rise in house prices was the increasing flow of funds being channelled into mortgage markets. During this period the Australian and New Zealand banks became increasingly reliant on overseas funding, with up to 40% of their funds sourced from overseas (RBA 2009a; RBNZ 2009a, b), and thus domestic credit expansion was increasingly tied to a more globalised flow of funds. In effect, the housing booms in Australia and New Zealand were financed by global money flows rather than domestic savings. The nature and impact of these flows differed from the US experience and helped to shape the domestic mortgage markets in very different ways.

In addition to the traditional bank sector, new lenders funded by the wholesale money market and using securitisation entered the Australian market. These new lenders, although accounting for a small part of the market, actively created a mortgage market for

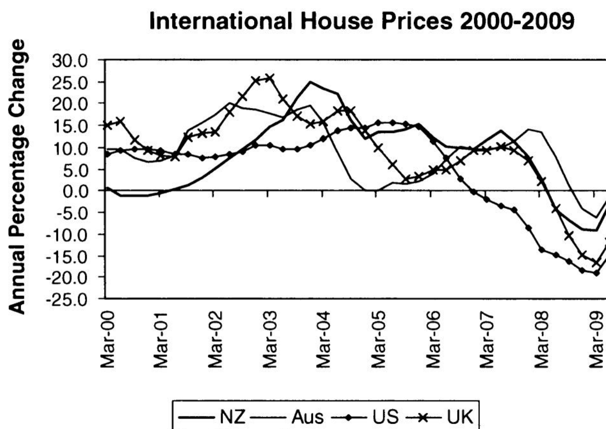

Fig. 1 International House Prices 2000–2009. *Source*: Adapted from Reserve Bank of New Zealand, Financial Stability Report November 2009, data file

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non-conforming mortgages, which were the Australian version of sub-prime mortgages. From the mid-1990s Australia developed "one of the largest (asset-backed securities) markets in the world" that in 2007 amounted to US$ 215 billion (Green and Wachter 2010, p. 425). The growth in the asset-backed securities market primarily reflected the growth in the issuance of residential mortgage-backed securities (RMBS), especially among regional banks that found securitisation to be cost-effective given that they had limited access to branch networks to access retail funds. As a consequence of these financial transformations, lending in the mortgage market became more liberalised and consumer focused.

The liberalisation of mortgage markets and the specific character of the tax system in Australia (that supported negative gearing[1] for investors) resulted in changes to the nature and character of borrowing (Yates 2009). In 2003, investors accounted for approximately 45% of new mortgage lending while first-time home-buyers accounted for only 14% (Berry and Dalton 2004). For the banking authorities the post-2001 housing boom was viewed as the product of speculative pressures, with large flows of capital directed into the housing sector. Rising housing equity withdrawal (Smith and Searle 2010) and the general wealth effect of rising house prices resulted in inflationary pressures and from 2003 interest rates began to climb. Rising interest rates led to declines in house price inflation but accessing home ownership remained problematic for first-time home owners. Indeed, Yates (2008) argues that in Australia private renters, who incur the highest incidence of housing stress, "face the prospect of never being able to gain access to the economic and social advantages provided by home ownership" (p. 212).

Financial deregulation in New Zealand from the 1980s meant that the Reserve Bank (RBNZ) had responsibility for containing inflation and discharged its responsibilities by managing interest rates. In an attempt to cool down the post-2000 housing boom the RBNZ raised the official cash rate by 325 basis points from 5% in 2003 to 8.25% in 2007. In lifting the cash rate in New Zealand to an internationally high level, well in excess of interest rates in the USA, Europe and Japan, the RBNZ created the conditions for a dramatic rise in the global demand for New Zealand dollar-denominated bonds (Uridashi and Eurokiwi bonds). As a consequence, retail investors in Japan and Europe engaged in unhedged carry-trades (borrowing in a low interest rate economy to invest in a high interest rate economy without hedging for changes in exchange rates) designed to access high yields. International agencies such as the World Bank issued Uridashi bonds and then entered into swaps with New Zealand banks seeking access to cheap funding. This money was used to fund the New Zealand mortgage market and in particular fixed-rate mortgage products. In contrast to the Australian mortgage market, where variable mortgage rates dominated, fixed rate mortgages of 1–5 years duration rose to dominate the New Zealand mortgage market. Whereas variable rate mortgages accounted for 93% of the New Zealand mortgage market in 1994, by 2007 fixed-rate mortgages accounted for 87% of the market (Murphy and Young 2008).

During this period fixed-rate mortgage products were priced below variable rates as interest rates on these products were determined not by the domestic official cash rate but by international swap rates. While consumers accessed cheaper mortgage rates the RBNZ's capacity to affect the mortgage market was increasingly diluted and it was increasingly placed in an invidious position. In order to dampen inflationary pressures arising from the housing and consumer boom it was forced to raise interest rates. However, raising interest rates created increased international carry-trade activities, which put upward pressure on

[1] Negative gearing occurs when the rental stream on a property is less than the investor's mortgage payment on the loan used to purchase the house. The investor's loss is tax deductible in Australia and New Zealand.

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the exchange rate and helped fuel cheaper fixed-rate mortgages. High domestic interest rates, and a high dollar, punished other parts of the economy, especially the export sector, but perversely created the conditions for the cheaper fixed-rate mortgages that supported the housing boom. The relatively aggressive stance taken by the RBNZ to halt the housing boom was thus undermined by the increasingly globalised nature of financial flows that funded the market. In New Zealand, on the eve of the GFC, the major housing problem was deemed to be housing affordability, or more specifically the cost of accessing home ownership (Badcock 2004; House Prices Unit 2008; Thorns 2009; Murphy 2009).

The US sub-prime crisis and the resultant GFC had limited direct impact on the Australian and New Zealand[2] banking system. According to the Reserve Bank of Australia (RBA) (2009a), Australian banks had few exposures to the sub-prime mortgage market, had not developed overly risky mortgage products and pursued relatively conservative mortgage lending practices. Indeed, during the crisis the Australian banks' credit ratings placed them in the top tier of banks in the world. Where the credit crunch had a direct impact was in the non-banking and wholesale-funded sector in Australia, and the finance company sector (the source of property development finance) in New Zealand. Yet, given the mainstream banks' reliance on overseas funding, the cost of funding and access to funding became problematic. In the wake of a major global crisis and rising liquidity issues, bank lending became more conservative and house prices began to drop in Australia and New Zealand in 2008.

5 Australian policy responses

In common with other industrialized nations, Australia was adversely affected by the banking crisis and the credit crunch. The most affected sectors of the mortgage market were the non-traditional lenders that had extended non-conforming mortgages. In direct response to the credit crunch, mortgage originators funded from the wholesale money markets crashed but the larger retail banks took their position in the mortgage market. Arrears on non-conforming mortgages increased to 4.5% in 2007, compared to only 0.25% for securitised prime mortgages, but non-conforming mortgages accounted for only one per cent of loans outstanding (Debelle 2008).

In February 2009, in response to the GFC, the Australian government introduced its AU$42 billion 'Nation Building Economic Stimulus Plan' (Australian Government 2009). The plan included a substantial Social Housing Initiative that involved over AU$5 billion expenditure on the construction of new social housing over 3 years and AU$400 million expenditure on the renovation of existing social housing. This long-term support for housing construction followed hard on the heels of a substantial increase in support for home ownership.

In relation to home ownership and housing affordability, the government introduced in the 2009/10 Budget a new First Home Owners Boost (FHOB). In addition to the existing first home owner grant, the FHOB amounted to an additional A$7,000 grant to first-time buyers of existing properties and an additional A$14,000 for first-time buyers of new houses. Under the provisions of the scheme, first-time home buyers of new houses could draw down A$21,000 in grants, which represented a substantial level of assistance for those struggling to generate a deposit on a house. The FHOB was introduced in October 2008, a month after the collapse of Lehman Brothers. The scheme was initially designed to

[2] Over 90% of New Zealand bank assets are owned by Australian parent banks.

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terminate in June 2009 but this was extended to December, with maximum payments of the FHOG and FHOB combined being reduced from October 2009 to A$10,500 for existing houses and A$14,000 for new houses (Plibersek 2009; RBA 2009b).

From October 2008 to the end of October 2009 a total of 190,050 new home owners availed of the boost (Plibersek 2009). As Fig. 2 shows, within the context of declining house prices and interest rates, the FHOB proved to be a very effective stimulus for new entrants into the market. Reflective of the more favourable conditions, in December 2008 first-time buyers, for the first time since January 2002 (see Fig. 2), accounted for 25% of all dwellings financed in Australia and accounted for 35% of owner-occupier loan approvals by September 2009 (RBA 2009a).

Within the context of a possible global residential property market crash, the FHOB and the Social Housing Initiative represented a substantial stimulus to the housing and construction sectors. In response to the stimulus, house prices in Australia began to rise again (see Fig. 3). In the year to September 2009 the Australian Bureau of Statistics reported an increase of 6.2% in house prices at a national level (RBA 2009b, p. 36). In contrast to the UK, USA and Irish experiences, the Australian housing market entered into potential boom conditions early in 2009. The relatively rapid recovery of the Australian economy in

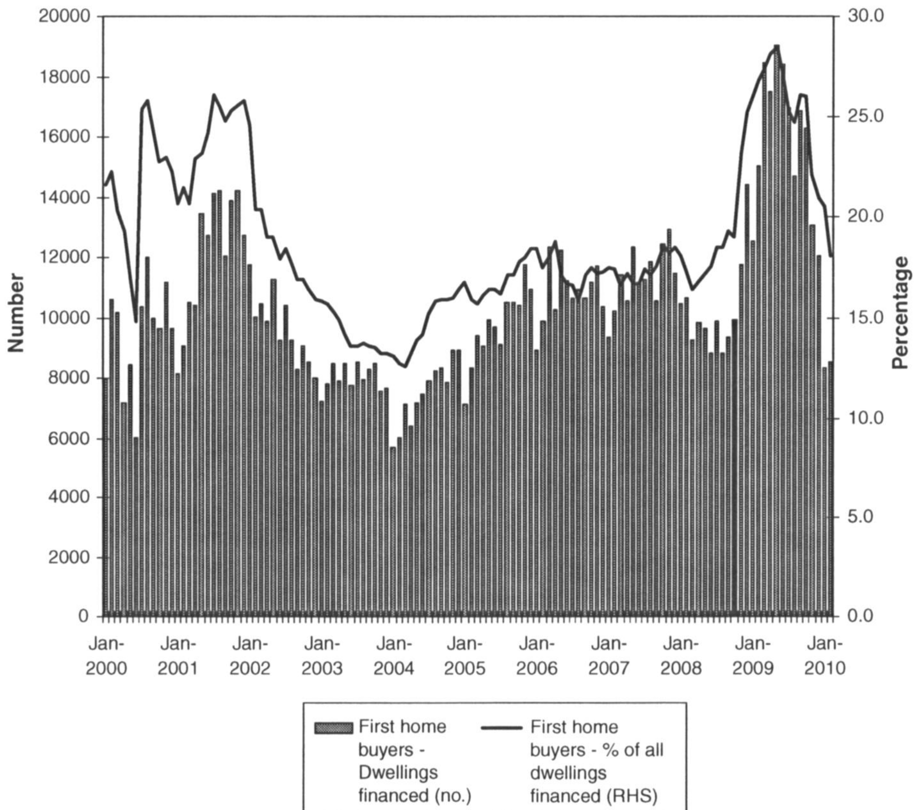

Fig. 2 Australia- First Home Buyers Dwellings Financed (Monthly). *Source*: ABS (2010) TABLE 9a. HOUSING FINANCE COMMITMENTS (Owner Occupation), By Type of Buyer and Loan: Australia, Original

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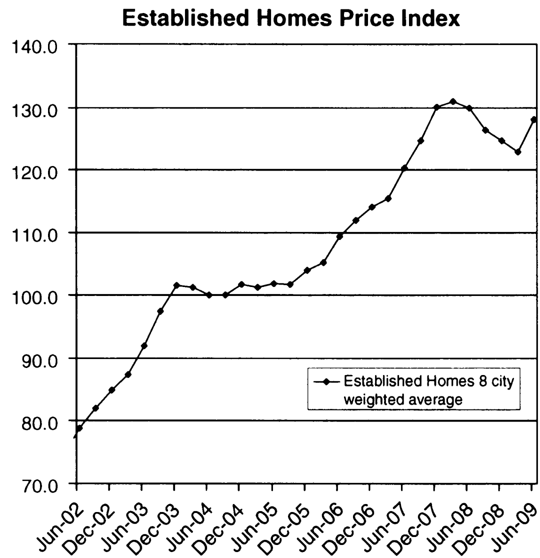

Fig. 3 Australia House Prices: Established Homes, 8 City Weighted Average (ABS 2009: 6416.0 House Price Indexes: Eight Capital Cities)

conjunction with the FHOB and the economic stimulus package meant that the impact of the crisis on the Australian housing market was rather shallow. Whether this constitutes a return to a long-term housing boom depends on the on-going economic prospects of the Australian and global economies.

6 New Zealand policy responses

In contrast to the Australian response to the GFC, which used investment in housing as part of a major fiscal stimulus package, the New Zealand government's reaction was more restrained and intervention focused primarily on the Reserve Bank's support for the banks. In a response to the financial crisis and the global credit crunch, the government introduced a bank guarantee. In addition, on July 1, 2009 the Government announced a $323 million *Warm Up New Zealand: Heat Smart* programme that offered home owners a non-means tested 33% subsidy on insulation (floor and ceiling) and a grant of $500 for installing a clean heating source.

The Reserve Bank, for its part, acted to stave off recession by aggressively decreasing the OCR. In a 9-month period, between June 2008 and April 2009, the OCR was reduced from 8.25 to 2.5%, the lowest rate ever offered. This resulted in a significant decline in variable-rate mortgage rates and improved housing affordability at a time when house prices had begun to fall in nominal terms (see Fig. 1). However, the immediate effect of a declining OCR on existing mortgagors was dampened, given that most households were on some form of fixed-rate mortgage.

In direct response to the credit crunch, in May 2008 the Reserve Bank announced a number of measures to ensure liquidity in the local banking sector. Of particular interest in relation to the housing market was the creation of a Term Auction Facility (TAF). Under the terms of the TAF, the Reserve Bank accepted AAA-rated residential mortgage backed securities as collateral for loans. At the time of announcement of this facility none of the major banks had active (mortgage) securitisation programmes (Nield 2008, p. 15) but by

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November these banks were well placed to access the facility. For the RBNZ, the TAF was designed to make it a lender of last resort, in a period of global illiquidity. In effect the TAF provided an opportunity for the creation of a mortgage-backed security (MBS) market for *high-quality* mortgages. Between November 2008 and March 2009 the banks accessed NZ$7.6 billion of funding and a further $NZ18 billion was available under the scheme (NZ House of Representatives 2009). The fact that the banks accessed this funding is illustrative of the difficulties that they faced in accessing funding in the global market.

Significantly, arising from the global liquidity crisis the Reserve Bank has introduced a new prudential liquidity policy that seeks to address the risks associated with the retail banks' reliance on the 'carry trade' as a source of funding. New Zealand banks are now required to make greater use of customer deposits and long-term markets to fund their mortgage operations. This move is designed to push up mortgage rates in the future and reduce the need to raise the official cash rate to dampen housing demand (Hoskin et al. 2009).

The rapid turnaround in the banks' capacity to access international funds, combined with the sudden drop in house prices (by 9%; see Fig. 1) and the broader spectre of a global economic crisis, altered mortgage market activities in New Zealand. Banks moved away from issuing high loan-to-value mortgages and increasingly required deposits of 20%. Mortgage defaults and arrears rose and there was increasing media concern regarding the potential for a rise in negative equity. However, in contrast to the US experience, the New Zealand market proved less susceptible to rapid rises in mortgage defaults. Impaired and past due assets, as a proportion of bank lending, increased from a low of 0.3% in 2004 to 0.8% in 2008 (IMF 2009). However, in an analysis of the robustness of the New Zealand mortgage market the IMF concluded that a mortgage crisis was unlikely. It argued that interest rates had fallen by over 400 basis points (which assisted households in servicing their loans), an important segment of high loan-to-value loans was insured by third parties and the New Zealand legal system made home owners responsible for any remaining debt even after repossession. In addition, the IMF argued that the overall structure of the mortgage market seemed robust given that:

> ... in 2007 approx 75% of mortgage debt was held by households with incomes in the two highest quintiles and their debt service ratio was below 20%. (And) Households in the two lowest income quintiles held only 7 percent of mortgage debt. (IMF 2009, XX)

While house prices dropped by 9%, the clearest manifestation of a housing crisis was the significant decrease in the volume of houses sold. From a monthly peak of 11,378 house sales in March 2004, monthly sales declined by almost 63% to 4,220 sales in September 2007 (Department of Building and Housing 2008). In line with Berry and Dalton's (2004) argument, it seems New Zealand homeowners responded to house price declines by staying put.

The tighter credit conditions and the decline in prices resulted in a very significant decline in building consents issued. As Fig. 4 clearly shows, there has been a rapid decrease in new building activity. Building consents for new dwellings (excluding apartments) declined by 30% from 2007 to 2008 and consents for all residential developments in 2009 were down 54% on the peak of 2004. Developers and investors, who had come to increasingly rely on finance companies as their funding source, were severely affected by the collapse of this sector.

While the credit crisis prompted a considerable restructuring of the development and building sectors, the downturn in new building has occurred during a period when housing

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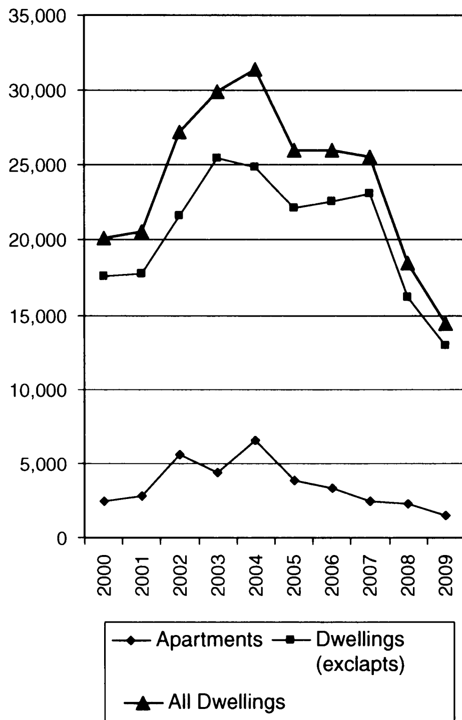

Fig. 4 New Zealand Annual Residential Building Consents (No.). *Source*: StatsNZ Building Consents Issued, various issues, Year end December

demand is likely to increase in coming years (DTZ 2009). Positive net migration combined with natural increase and changing family formation structures means that there exists a strong demand for new houses and this is particularly evident in regional housing markets. Depending on the broader performance of the economy, and particularly unemployment, it is arguable that the housing downturn in 2008 provided a potential context for a new housing boom. Indeed, recent data on house prices (Fig. 5) show that prices rose again in 2009 and in March 2010 average prices were only 3.9% below the market peak of late 2007 (QV 2010). In Auckland, the largest metropolitan region, house prices rose by 9.9% over the year to March 2010. Whether these price rises constitute a short-term bounce or the beginning of a new boom is difficult to ascertain but it does highlight a degree of house price resilience in the housing market, a point not lost on home owners and investors.

7 Conclusions

Given the significant price booms that occurred in residential property markets around the world, and that the GFC had its origins in the problems of the US sub-prime mortgage market that emerged in 2007, it is not surprising that the spectre of a global housing market crash loomed large in early analyses of the crisis. This potential meltdown of the housing market had particular resonance for politicians and policy makers. However, the evolving narratives of a potential global housing market crash tended to elide the reality of nationally constituted housing markets characterised by different demand and supply conditions. While Australia and New Zealand's house price dynamics have mirrored (particularly in the upswing phase) other markets, they have differed in terms of the

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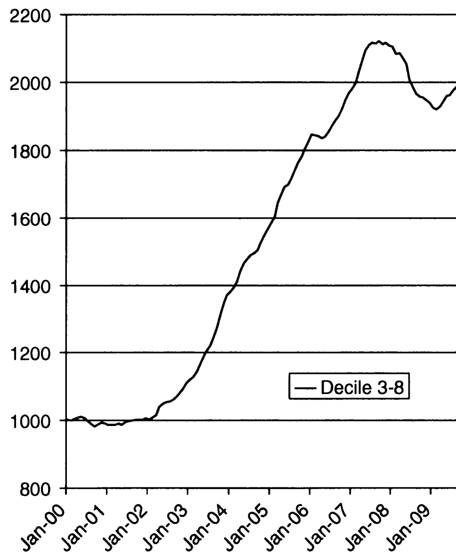
Fig. 5 New Zealand House Price Index (Houses in Decile 3–8 Range) (RBNZ: FSR Nov 2009 Data File Table Data D1)



intensity and timing of the downturn. Moreover, the institutional structures and dynamics of market actors, and in particular the operation of financial institutions, have profoundly affected the ways in which these national housing markets have been affected by the GFC.

The Australian and New Zealand housing markets have experienced downturns in the wake of the GFC but the magnitude of their price declines has been relatively minor compared to the problems of countries such as the USA, the UK and Ireland. While both countries had undergone a significant liberalisation of their mortgage markets, their banking sectors were not directly exposed to the US sub-prime market, nor had they developed the risky products evident in the US market (e.g. negative amortisation and teaser rates). Having said that, the GFC created significant liquidity problems for banks around the world and increased the cost of funds. Given that the Australian and New Zealand banks are heavily reliant on overseas funding they were impacted by the crisis and this has affected their mortgage activities.

The policy responses to the crisis have been significant and different. In Australia, the government introduced a large fiscal stimulus package that included a significant housing component. The stimulus package involves renewed support for the social rented sector and significant support for first-time home owners. The immediate effect of the boost has been to encourage large numbers of first-time buyers to enter the market and this in turn has acted to put upward pressure on house prices throughout 2009. Arguably the policy response has addressed an important component of the affordability problems faced by first-time buyers by addressing the deposit gap. The effect of these types of grants is to "bring forward the purchase decisions of these first-time buyers" (Wood et al. 2006, p. 27). In the short run the policy has been successful in getting people into home ownership and in helping to avert a serious property crash. However, the medium- and long-term consequences remain to be seen. It is possible that recipients of the FHOB are vulnerable to negative equity given that the boost will not be available to first-time buyers in the future and this may have an adverse effect on first-time buyer demand and future house price dynamics.

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In New Zealand the government has been less profligate in its support of housing and much of the response to the crisis has been mediated by the Reserve Bank. The official cash rate was reduced to its lowest ever level in order to stimulate the economy and this had a significant effect on mortgage interest rates. In addition, the Reserve Bank has provided various liquidity measures aimed at ensuring the viability of the banking sector and, in turn, the housing market. Overall, the New Zealand policy and regulatory responses to the GFC have centred on supporting the banks and moderating the adverse consequences of a housing downturn. While policy makers have eschewed direct support for the housing market, the RBNZ was forced to respond in a manner that ultimately supported the housing market and sought to ensure market stability.

In reflecting on the Australian and New Zealand experiences it is arguable that national governments and monetary authorities have become mired in a policy dilemma. While support for home ownership remains strong it is recognised that a booming housing market not only creates affordability problems and issues relating to access, but it also, though equity withdrawal, fuels consumer booms that place pressures on the macro-economy. However, the wealth effect of a housing slump is also problematic and thus governments, and especially the Australian government, have been keen to support the housing market. Although Australia and New Zealand have adopted different responses to the financial crisis, it is clear that the macroeconomic significance of home ownership has meant that house price booms, or at least moderate price growth, have become an institutional/political imperative. It is significant that the interventions that have occurred in Australia and New Zealand have supported renewed house price growth that may constitute the basis for a new housing boom.

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ABS. (2010). 5609.0—Housing Finance, Australia, Feb 2010: TABLE 9a. Housing Finance Commitments (Owner Occupation), By Type of Buyer and Loan: Australia, Original, http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5609.0Feb%202010?OpenDocument. Retrieved 29/4/2010.

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