# HOT TOPICS – PARLIAMENTARY HEARINGS – 15 & 17 FEBRUARY 2023

## Monetary policy

- Assistant Treasurer Stephen Jones said he hoped the February rate hike was nearly the last, if not, the last. Are we near the peak yet? Are comments like that from the Government detrimental to your cause? Should the Government refrain from commenting?
- Markets are pricing in a cash rate of 4 per cent by June and some economists are pricing a 3.85 per cent terminal cash rate. Does the RBA have a view on the terminal cash rate given its inflation forecasts?
- The latest retail sales data suggested consumers are tightening their belts and we know many households will be hit as their fixed-rate mortgages roll over to variable rates this year. Given you've already done so much, isn't now the time to pause and see the impact of those rate hikes? Why go on punishing ordinary Australians?
- Your aggressive rate hike cycle will tip the economy into recession. Why can't you see that?
- The Treasurer has called on banks to pass on higher interest rates to savers. Do you agree and will you back that call? What is your view of banks who have failed to pass on rate increases to depositors?
- When do you expect the lag effects from recent interest rate rises will start to take effect on households in Australia?
- Former Treasury adviser Stephen Anthony said the chance of a recession next year could be as high as 70 per cent due to the impact of the RBA's high interest rates, coupled with a slowdown in key markets such as China. Can you comment on this prediction?
- Economic data is giving us a mixed picture of the economy locally and globally. What factors/data are you focussed on at this time (apart from CPI)?
- How are you using the monthly CPI in your monetary policy considerations and forecasts?
- What are the risks that inflation will become more entrenched? How will the RBA respond if this occurs?
- Many people argue price pressures are coming from cost inputs not demand, and increasing interest rates won't have any effect on inflation. How do you respond?
- Did central banks contribute to the current inflation problem by encouraging people to take on more debt and flooding the economy with cheap cash?
- You previously said the current high inflation is expected to be relatively short lived. If that's the case, why have you been raising rates so aggressively? Can't you just let inflation sit above target for a little while until it resolves itself rather than inflict more pain?
- The RBNZ has raised its policy rate to 4.25% and they have inflation levels similar to Australia. Our cash rate is well behind. Can you explain why we are taking a less aggressive approach?
- The US central bank raised its federal funds rate by 25 basis points this month to a target range of 4.5-4.75 per cent. How far behind is Australia in its tightening cycle than the US?

- How do you determine the balance between meeting your inflation target and your mandate to contribute to the economic prosperity and welfare of the Australian people? Will you sacrifice inflation staying higher for longer to keep unemployment low, avoid a recession and avoid mass mortgage defaults? What trade-offs are you willing to make?
- Are there other approaches that could be taken to reducing inflation?
- How do you expect people to put food on their table or keep a roof over their head?
- What can be done to stop price gouging by businesses?

## Government/Budget

- Are fiscal and monetary policy working in tandem or at odds at the moment?
- What do you want to see in the upcoming Federal budget?
- The Government needs to help ease the cost of living pressures but that could work against your efforts to bring inflation back down to target. We know you don't give advice to the Government, but is it fair to say interest rates will have to be higher and stay higher for longer if the Government provides more fiscal support?
- If the government was to cut back on spending in its budget, would that help reduce inflation? What impact does government spending have on inflation and should the government be focused on returning the budget to surplus?
- Will the Government's intervention in the energy market bring down inflation in any meaningful way?
- What impact would you expect tax cuts to have on inflation?
- Many people are calling for the stage three tax cuts to be scrapped. Won't putting more money into the hands of the wealthy be inflationary and entirely the wrong thing to do right now?

## Wages/employment

- Wages aren't keeping pace with inflation which is also putting pressure on household budgets. If inflation becomes entrenched and wages don't rise, are we headed for a recession?
- In December, you encouraged people to take a real wage cut by accepting increases below 4 per cent in order to avoid a wage price spiral. How are people meant to respond to that? Are there better solutions in the form of other targeted support?
- Are you concerned with the impact higher rates will have on employment? Are people going to lose jobs?
- Do you think there are institutional or structural factors in Australia that are keeping wages at a lower level than elsewhere?
- What evidence do you have that businesses are lifting, or intend to lift, wages? Are you relying on this information from a small number of firms in the liaison program?
- Do you support the return of immigrants to the country? Will this alleviate wage pressures and therefore inflation?

- The ACTU is likely to push for an increase to the minimum wage and the government is said to be considering an increase to JobSeeker in the May budget (from $334.20/week to $511/week if ACOSS gets what it wants). How will this affect inflation?
- The ABS noted that the previous increases to minimum wages were starting to show in the CPI data, along with other wage increases in labour intensive services sectors. Is this an indication that a wage-price spiral has kicked off? What will the impact be for households?
- TheAustralian Government is trying to pass legislation that would allow unions to pursue pattern bargaining and drive wage increases not backed by productivity gains across industries. Are you concerned about the legislation being passed in the current high inflation climate? Would this stoke wages growth and increase inflation even further?

## Housing/mortgages

- What is the Bank's expectation for consumption and inflation when the fixed rate mortgages role off?
- There is significant reporting on a mortgage cliff in 2023 when fixed rate mortgages roll off in 2023 and 2024. Marion Kohler recently said more than 800,000 loan facilities worth $350bn are due to roll off fixed rates in 2023. Can you clear this up and confirm if you expect there will be a mortgage cliff and what the impact will be on the economy?
- How can the Bank raise rates the right amount when it does not know how many households are going to be hit by the expiry of fixed rate loans? (And similarly) What is the geographic distribution of the fixed rate cliff?
- Does this looming runoff make it harder to know when tighter monetary policy will have an impact?
- Did APRA's removal of the 7% floor in loan serviceability assessments contribute to the current high levels of people potentially at risk of defaulting now rates have gone up?
- Are you concerned that you now appear to have increased rates past the buffers that the banks had in place? Is it reasonable to consider stopping at this time?
- Would the RBA support APRA relaxing the serviceability buffer to support Australian borrowers seeking to refinance?
- Should the banks be held responsible for allowing borrowers to borrow amounts that are now beyond their means?
- Do we have a structural issue caused by the large volumes of variable rate mortgages? Would having a majority of owner occupiers on fixed rates for the life of their mortgages (similar to the US) be a way to fine-tune the inequitable effect of monetary policy on the general public?
- Is tighter monetary policy impacting rents? Data shows rental listings fell more than 25 per cent in 2022 while rents rose 10 per cent across capital cities. Many investors have enjoyed much bigger rent rises as tenants battled for scarce accommodation, and asking rents have surged again in January and are up 18 per cent year-on-year. What's the solution to this inequality?
- What is the likely impact on small businesses that have used mortgages on fixed rates to fund their business?

## Financial Markets / BPP

- There's about $200 billion of bank funding rolling off in the next 12- 18 months. What modelling or forecasting has the RBA done on the impact of that on bank funding costs and the flow on effect to households? Will it drive out-of-cycle rate hikes? Would that be something the Bank would want to rule out?
- Does the RBA know what proportion of fixed rate mortgage are a direct result of TFF funding?
- Was the TFF effectively a subsidy for the Banks? Is it appropriate to still be subsidising the banks now while making mortgages more costly and tightening the screws on households?
- Did the TFF directly contribute to the inflation levels we are experiencing now?
- The Bank is currently in a position of negative equity. Is the Bank still exposed to the risk of more losses if yields move even higher as a result of high interest rates? Do you have forecasts on these expected losses?
- The Bank has experienced a $21 billion loss. Based on accounting forecasts how big will this loss be at the end of the 22/23 FY if interest rates align with market expectations of around 4 per cent by mid 2023?
- In the BPP Review paper there are four ES rate scenario projections to show the direct effect of different paths of policy rates on the Bank's earnings. It seems more likely it could be 3½ per cent or 4½ per cent beyond 2023. Can you comment on the bank's earnings if these scenarios eventuate?
- How long will it take for the Bank to go into positive equity?
- What impact does the depreciation of the AUD against the USD have on Australian consumer prices and what do you expect to happen to the AUD in 2023 as the US continues to tighten? What impact will this have on exports?

## Payments

- What is the cost of producing a retail CBDC?
- Have you considered how the Bank will phase out cash if it releases a retail CBDC?
- What is the timeframe for the Reserve Bank issuing a retail CBDC?
- What are the regulatory gaps for the introduction of a retail CBDC or a wholesale CBDC?
- There seems to be a view that the PSB is scrambling to stay ahead of payments innovation in general, particularly when it has lack of access to payments data from the commercial banks and big tech companies such as Apple Pay etc. What is your view on this?

## RBA Review

- What has been the internal response to the review from staff at the Bank? I understand staff were invited to complete a survey. What has the response rate been and what types of comments are they making?
- At what stage is the RBA Review at now and when do you expect to receive a preliminary report? How long is the review expected to take?

- You set up panels of private-sector economist and academics. Was this in response to the RBA Review? How were participants chosen?
- What kind of outcomes is the RBA anticipating from the review? i.e. a change in the inflation target or changes to the structure of the Board?

## $5 redesign

- Why can't we honour First Nations and the Monarch on the same banknote? Did you consider this option?
- This decision is a snub to our heritage. Why elevate one culture above another?
- We are a constitutional monarchy, why is it not appropriate for the Monarch to be featured on one of our banknotes?
- You've said this matter has intense national interest, why then did you not seek public opinion first? Why did you seek only the opinion of the Labor Government? Did you do this at the behest of the Labor Government?
- Which First Nations group have you consulted so far and how will your consultation with First Australians look like? How are you going to make sure it is inclusive? How long is this consultation process likely to take?

## Others

- You received some public backlash for your apology at Senate Estimates to mortgage holders who acted on the Bank's forward guidance and some are calling for a class action and your resignation. Are you still sorry and do you still accept responsibility?
- At least four Labor MPs (Rob Mitchell, Jerome Laxale, Julian Hill and Graham Perrett) have suggested your seven-year term should not be extended. Do you think these MPs are undermining the independence of the RBA by making such populist comments?
- Do you think your term should be extended like your two predecessors? Or do you agree that your misjudgement on rates has cost you your job? What should the Treasurer take into account when considering whether to extend your term?
- Senator Nick McKim has called for your sacking and for the Government to reverse the latest rate hike decision. What would you say to that? Does the Government have the power to do that?
- A lot of people have noticed building works at the RBA. Can you explain a bit about the cost of these building works?
- Do you think now is a good time for the RBA to embark on building works when we are on the brink of a recession? How can you justify the cost?
- I heard you have discovered hazardous materials in the building and are no longer planning to remain in the building during the works. How much more is the project costing due to the hire of external office space?
- You have described the setback in the ASX CHESS replacement program as disappointing and urged the exchange to prioritise delivery of a new clearing/settlement infrastructure. At the same time you

urged the exchange to maintain a legacy system that is no longer fit for purpose in this day and age. It will take many years before a viable replacement is in place. What timeframe is acceptable? With your financial stability lens on, do you see a cyberattack on the obsolete technology as a major risk, what other risks do you see in the meantime?

- What were the latest findings from the Bank's audit of its gold holdings at the BoE? Was all the gold there? How much does the Bank hold at the BoE versus as in Australia?
- What is the RBA doing towards making its own climate disclosures? Why isn't the RBA doing as much as other central banks on climate change?
- What's the Bank's views on the government's climate change policies?
- There have been calls for the Governor to resign by several public figures. What do you make of this? If the Governor does resign after the review, will you step in as Governor?

# EXPIRING FIXED-RATE HOUSING LOANS (DETAIL)

- **By value:** ~30% housing credit is fixed rate (~$650bn)
  - ~½ fixed-rate loans expire in 2023 (~$350bn)
  - New fixed-rate lending share very low (~5%)
- **By number:** APRA data on facilities **NOT** borrowers; ~¼ facilities fixed (~1.6m) and ~½ expire in 2023 (~880,000).

**Annual** Maturity Profile – Aggregate APRA data

| | Stock as at Dec 2022* | Of which, will expire in: 2023 | 2024 | 2025 and after |
|---|---|---|---|---|
| **By value outstanding** | | | | |
| Value ($b; rounded) | 650 | 350 | 200 | 100 |
| Share of all housing credit | 30% | 15% | 10% | 5% |
| Share of fixed-rate credit | | 54% | 30% | 16% |
| **By number of facilities** (**NOT** #borrowers)** | | | | |
| Count (‘000; rounded) | 1,630 | 880*** | 450 | 300 |
| Share of all housing facilities | 25% | 14% | 7% | 4% |
| Share of fixed-rate facilities | | 54% | 28% | 18% |

* In 2022 around $210bn or 590,000 loan facilities rolled off fixed rates.
** Borrowers may have >1 facility; excludes fixed-rate loans part of a split facility if fixed-rate a/c balance < variable-rate a/c balance. Data by value includes fixed-rate portion of split facilities.
*** Estimate given in Cost of Living testimony: 800,000 to high 800,000s; media quoted 800,000.
Sources: APRA; RBA

- **Data:** APRA aggregates offer best coverage; Sec data ~1/3 credit but > granularity.
- **Frequency:** Sec shares ≈ APRA **semi-annual**; monthly not confident is reliable
- Fixed-rate expiries to peak over 2H23 (~480k facilities expiring).
- **Geographic variation:** annual roll-off similar across states/territories and capital cities vs. regions.
- APRA *loan facilities* vs. Sec *loan accounts.* Loan facility = sum of all loan accounts borrower has with specific lender.

**Semi-annual** Maturity Profile **–** Securitisation Data

| | 2023 H1 | 2023 H2 | 2024 H1 | 2024 H2 | 2025 H1 | 2H25 & after |
|---|---|---|---|---|---|---|
| # a/cs (%)* | 26 | 31 | 13 | 13 | 11 | 5 |
| Applied to APRA facilities (‘000) | 400 | 480 | 225 | 225 | 205 | n/a |

* Share of loan accounts w/ expiring fixed rates. Annual shares ≠ APRA shares.
Sources: Securitisation System; APRA RBA

**Annual** Profile by **State and Territory** – Securitisation Data
Share of loan accounts with expiring fixed rates (%)

| | NSW | Vic | Qld | SA | WA | Tas | ACT | NT |
|---|---|---|---|---|---|---|---|---|
| 2023 | 58 | 61 | 53 | 54 | 56 | 53 | 57 | 54 |
| 2024 | 26 | 24 | 27 | 27 | 25 | 28 | 27 | 27 |
| 2025 and after | 16 | 15 | 20 | 19 | 19 | 19 | 16 | 19 |

Sources: Securitisation System; RBA

**Hypothetical ↑ in Loan Payments for Avg Owner-Occupier Fixed-rate Borrower***

| **Loan size** ($, 25y term) | Mth sched pmt at Feb 23 ($) | ↑ from Apr 22 ($) | ↑ from Apr 22 (%) |
|---|---|---|---|
| 350,000 (~avg. outstanding) | 2,200 | 640 | 41% |
| 500,000 (~ avg. @ origination) | 3,150 | 920 | “” |
| 1,000,000 | 6,300 | 1,840 | “” |

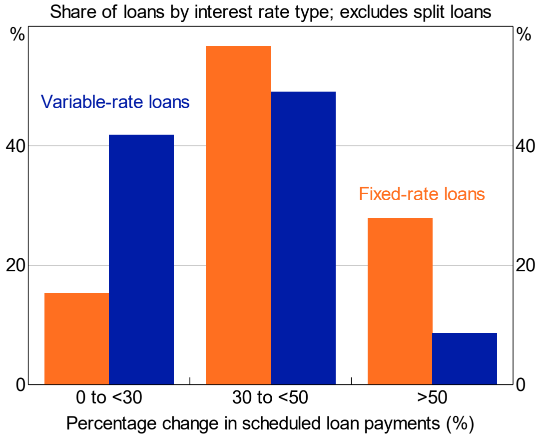
* Assumed to roll-off from average fixed-rate (~2.5%) to average outstanding variable rate (Dec 22 + full Feb increase: 5.85%).

**Key Facts from Bulletin**

- **Change in interest rates**: avg pandemic loan ~2.5% → roll off ~avg outstanding var rate (+325bps).
- **Increase in total repayments**: Most fixed-rate loan payments ↑ >30% at expiry (using cash rate at Feb 23).
  - Larger ↑ payments because fixed-rates < var-rates before tightening started.
  - Share of loans with Loan Servicing Ratio > 30% ↑ from 5% to 20% after fixed-rate expires.
- **Slightly risker:** fixed-rate loans newer, higher loan-to-income + LVR than var-rate loans. ↑ share FHB.
- **Prepayment buffers**: ⅓ fixed-rate loan >3mths (if roll-off immediately); ⅔ for var-rate and split loan (fix + var). Fixed-rate borrowers restricted from saving in mortgage; other evidence = have savings elsewhere.
- **Payments avoided:** ¾ loans avoided >3mths of payments vs. var-rate loan since Apr 22.
  - Longer time loan has rate fixed, greater benefit.
  - Maybe saved some payments avoided to prepare for higher rates (or spent them).
- **Small-business credit** very small (total stock = ~6% of housing credit). No ↑ small biz lending w/ fixed rate during pandemic (steady at ~1/3 of stock); ~½ all small biz credit secured by resi property. Small biz fix for diff reasons to housing borrowers; small biz panel suggest access to finance not price typically greater challenge.

**Increases in Scheduled Housing Loan Payments***

Share of loans by interest rate type; excludes split loans

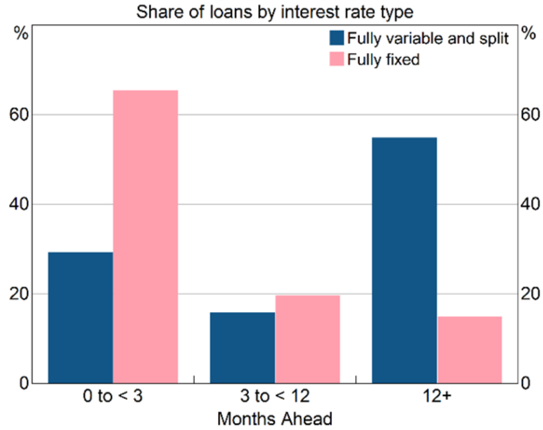



* Assumes variable rates increase to the outstanding variable rate in December plus changes announced as at February 2023 Board meeting. Fixed-rate loans are assumed to roll off to the same terminal rate. Payment increases do not incorporate rate discounts from refinancing to another lender or negotiating with existing lender.

Sources: APRA; RBA; Securitisation System

**Household Mortgage Prepayment Buffers***

Share of loans by interest rate type



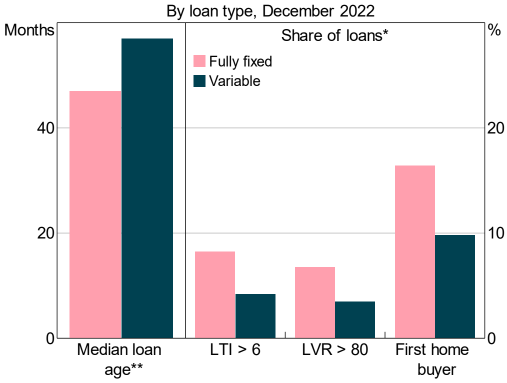

* Number of months that prepayments (offset and redraw balances) could cover a loan's minimum scheduled payment. For variable-rate loans this is calculated using the loan's current variable interest rate, for fully fixed and split loans this is calculated using the average new variable rate.

** Owner-occupier loans in December 2022.

Sources: APRA; RBA; Securitisation System

**Borrower Characteristics**

By loan type, December 2022



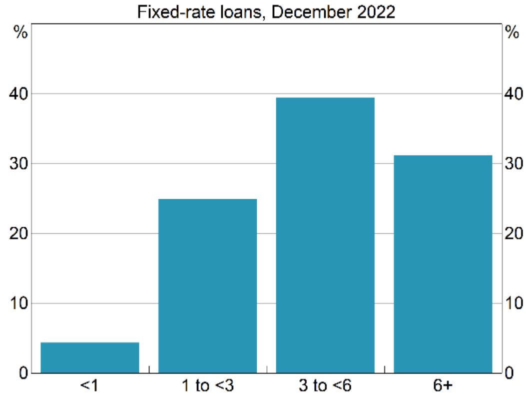

* LTI ratio is loan balance adjusted for prepayments (including offset balances) divided by an estimate of current income. LVR is scheduled loan balance adjusted for prepayments divided by an estimate of current value of the property. Current income estimated by growing income at origination forward by wage prices index. Property valuation at origination adjusted using house price changes at SA3 level.

** Excludes internally refinanced loans.

Sources: ABS; CoreLogic; RBA; Securitisation System

**Months of Repayments Avoided***

Fixed-rate loans, December 2022




* Calculated each month using the difference between loan's current scheduled payment at its fixed rate and the scheduled loan payment they would face at the outstanding variable rate from May 2022 until expiry. Expressed in months of new scheduled loan payment borrower is projected to face at expiry (using outstanding variable rate and market path for cash rate).

** Excludes split loans and loans that are worse off on their fixed rate.

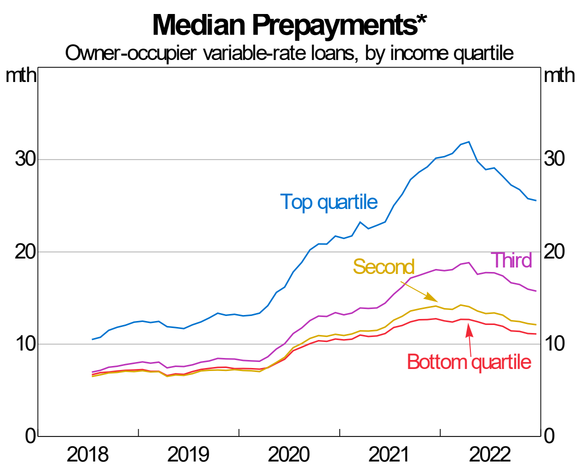
Sources: APRA; RBA; Securitisation System

# MORTGAGE RISKS TO FINANCIAL STABILITY – FEBRUARY 2023

## Overview

- Median prepayments (measured in months ahead) have declined across the distribution (Graph 1). Some of this decline is mechanical; monthly payments have increased in line with interest rates.
- Lower income borrowers are accumulating prepayment buffers at a faster rate than higher income borrowers (Graph 2).
- Less than a third of owner-occupier variable rate loans have fewer than 3 months' worth of prepayment buffers (Graph 3).
- Less than 2 per cent of loans are low income (lowest quartile) and high LTI (>6x) (Graph 4).

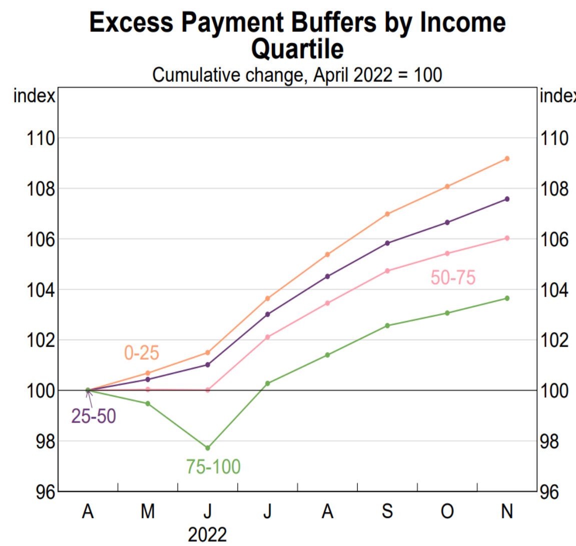
### Graph 1




* Months ahead expressed as number of months that prepayments (including offset and redraw balances) can cover minimum scheduled payments.

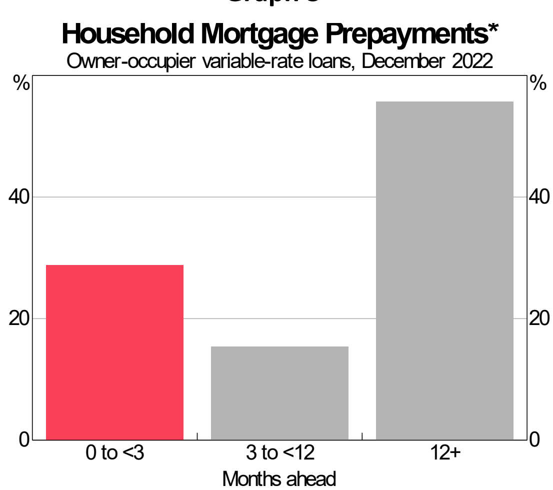
Sources: ABS; RBA; Securitisation System

### Graph 2




Source: RBA; Securitisation System

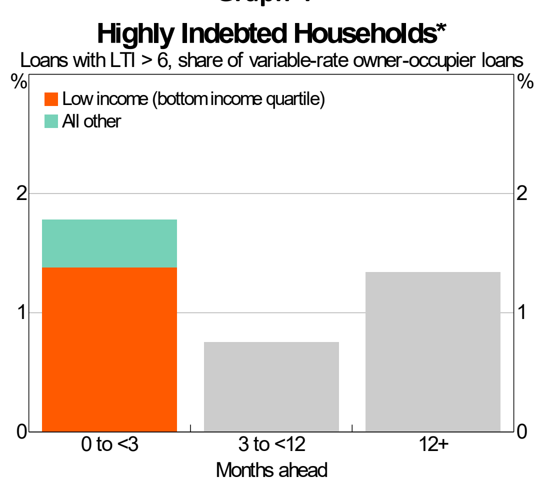
### Graph 3




* Months ahead expressed as number of months that prepayments (including offset and redraw balances) can cover minimum scheduled payments.

Sources: RBA; Securitisation System

### Graph 4



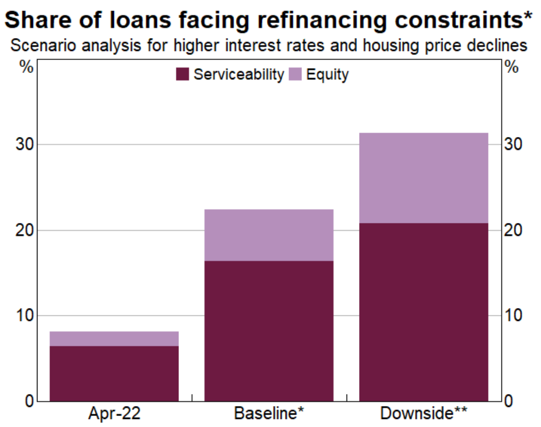

* Loan-to-income (LTI) is measured as the ratio of households' current loan value (net of redraw balances) relative to current income. Months ahead expressed as number of months that prepayments (including offset and redraw balances) can cover minimum scheduled payments.

Sources: ABS; RBA; Securitisation System

**Refinancing**

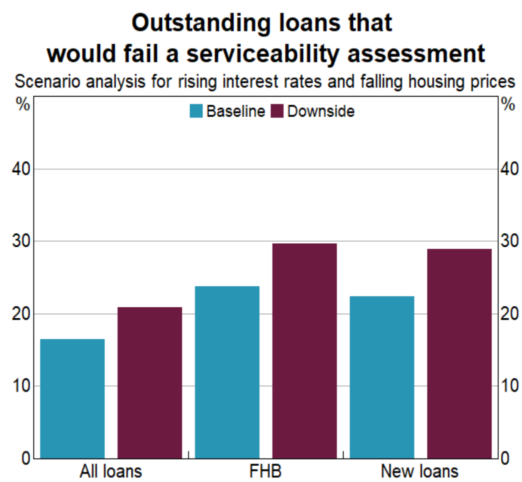
- In April 2022 a small share of existing loans (6 per cent) would have been unable to pass a lender's serviceability assessment. This share is expected to rise to around 16 (21) per cent in response to a 350bps (450bps) cumulative increase in the cash rate (Graph 5).
- An additional share of borrowers (those with an outstanding LVR >80) is expected to yield little to no economic benefit from refinancing their loans. This share is estimated at 6 (11) per cent of borrowers if housing prices fall a further 10 (20) per cent from end-December 2022 levels.
- Newer loans and FHBs are most vulnerable to refinancing constraints.
- Fixed-rate loans have been rolling off onto rates broadly in line with average outstanding variable rates, and more recently, average new variable rates (Graph 7).

**Graph 5**



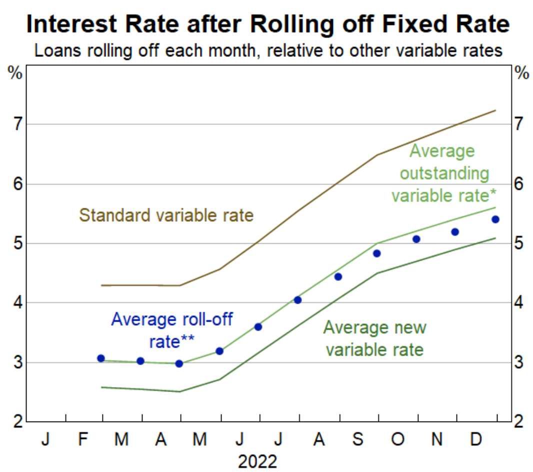

* Serviceability constraint denotes loans unable to pass a lender's assessment. Equity constraint denotes loans (outstanding LVR>80) expected to incur material costs to refinancing (excludes loans already serviceability-constrained).
** Assumes cumulative rise in the cash rate of 350bps and a 10 per cent decline in housing prices from end-December 2022 levels.
*** Assumes cumulative rise in the cash rate of 450bps and a 20 per cent decline in housing prices from end-December 2022 levels.
Sources: RBA; Securitisation System

**Graph 6**




* Assumes cumulative rise in the cash rate of 350bps and a 10 per cent decline in housing prices from end-December 2022 levels.
** Assumes cumulative rise in the cash rate of 450bps and a 20 per cent decline in housing prices from end-December 2022 levels.
Sources: RBA; Securitisation System

**Graph 7**




* For existing borrowers.
** For borrowers previously on fixed-rates (including split rate loans).
Sources: RBA; Securitisation dataset