

Low-doc loans can mean the difference between owning a property or not for a self-employed borrower

4th October 2007 – The market for low-doc loans is expected to continue to grow in Australia despite the likelihood of increased interest rates and broker regulation, according to Lenders Mortgage Insurer, Genworth Financial (Genworth).

Issue 3 of Genworth’s Spotlight Series discusses the emerging trends of low-doc lending in Australia, stating that the main factor driving demand for this type of mortgage is the growing number of contract and self-employed workers in Australia.

According to Issue 3 of Genworth’s Spotlight, the inception of the low-doc loan has provided greater opportunity for the self-employed borrower to purchase a home. With statistics showing that over 39% of the current Australian workforce is deemed to be self-employed, it’s obvious why demand for this product has grown.

Low-doc loans vary from mainstream mortgage products because borrowers self-certify their income and therefore their ability to repay the loan, because, unlike PAYG employees, they cannot produce regular pay-slips due to the nature of their work.

“While the number of lenders offering low-docs is now quite saturated – most banks and non-banks have a number of variants in their portfolios – the changing face of Australia’s workforce will continue to drive demand for this type of product,” said Peter Hall, Country Executive & Director, Genworth Financial Australia and New Zealand.

Hall said there is greater risk associated with offering loans to this group. But with proper safeguards in place, and risk offset by LMI, the opportunities for prudent lenders should continue to expand.

“While the product has an arrears rate approximately double that of a comparable standard loan, this does not necessarily translate into the same proportion of increased claims,” said Hall. “The higher arrears rates we see reflect the type of borrower the product is designed for – a borrower with irregular income from month to month. As a result, we see a higher cure rate for low-doc loans compared with standard loans that fall in arrears for very different reasons.”

Due to the US experience, there is some confusion about the difference between prime low-docs and sub-prime low-docs, which are designed for credit impaired borrowers and feature higher interest rates.

The vast majority of low-doc loans issued in Australia are prime low-docs, insured by Lenders Mortgage Insurance (LMI) providers such as Genworth Financial, and generally limited to an 80% Loan-to-Value-Ratio (LVR). Borrowers must also have a clear credit history and are required to self certify their income.

“As events in the US Sub-Prime market continue to play out, we do expect to see this negative speculation continue in the capital markets in relation to the Australian mortgage market in the short term,” Hall said. “However, we expect to see this subside and confidence restored in the medium term.”

Genworth identified three key indicators to check whether a borrower is suited to a low-doc loan:

- 1. Does the borrower have demonstrated cash flow?** Tax returns, financial statements and self-certification must accurately reflect their financial position.
- 2. Do the borrower’s assets and liabilities reflect their self- certification?** Does the actual nature of their self-employment look suspicious?
- 3. Does the borrower’s credit bureau look right?** Past applications for credit and approval success should be examined as well as looking for defaults and judgements.

About Genworth Financial

Genworth Financial is a leading financial security company meeting the retirement, longevity and lifestyle protection, investment and mortgage insurance needs of more than 15 million customers. It has a presence in more than 27 countries.

About Lenders Mortgage Insurance (LMI)

LMI is one of the most popular ways to achieve the dream of home ownership sooner for borrowers that do not have a large deposit.

Many Banks and Lending institutions require borrowers to contribute a 20-30% deposit before they will agree to provide a loan. LMI protects lenders against a loss should a borrower default on their home loan. If the security property is required to be sold as a result of the default, the net proceeds of the sale may not always cover the full balance outstanding on the loan. By using LMI, lenders are able to pass on this risk to a mortgage insurer such as Genworth Financial, which in-turn, enables them to offer the same loan amount but require less deposit.

For further information, call Emma Rumble, Marketing Leader on 61 2 8248 2227, or visit www.genworth.com.au.