Streets Ahead

Genworth Homebuyer Confidence Index

March 2011 • Second Edition

The right partner makes all the difference

Genworth® Financial

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Welcome to Streets Ahead: Second Edition

Confidence in the property market is always a hotly contested topic. As Australia's largest and oldest lenders mortgage insurer, Genworth Financial (Genworth) has been observing homebuyer attitudes and appetite for this market for over 45 years. We recognise that the property market underpins our economic prosperity as a nation and the personal wealth of many Australians. That's why we developed the Genworth Homebuyer Confidence Index (Genworth HCI); a biannual measure of confidence levels among Australian homebuyers and aspiring borrowers, which provides lenders, policy makers and consumers with valuable insights on what is happening in the mortgage industry across the country.

In this latest edition of the Index we find that the devastating natural disasters that have afflicted the nation throughout the past summer have caused homebuyer confidence to fall. As is to be expected, negative sentiment in Queensland and Western Australia has driven this change. The floods in Queensland have also driven up food prices which in turn has dampened confidence in other states. What we find as a consequence is that the rising cost of living is overtaking rising interest rates as the primary concern for borrowers across the country.

These findings reflect what our hardship data is showing us, with the number of applications for hardship spiking over the first three months of 2011. Flood-affected borrowers are telling us they expect to struggle for longer, so we are in the process of developing Hardship Solutions initiatives to meet these changing needs. We are working closely with lenders to provide more relief to borrowers whose financial situation has been adversely affected by natural disasters in general.

It is heartening to find that over 60% of borrowers who have accessed their lenders hardship programs are satisfied with this service. However, there is still much work to be done in improving general awareness of these support programs as recognition of them remains low, at just under 40%.

Consumer sentiment may fluctuate, but what we know for certain is that borrowers who contact their lender early when faced with financial difficulties are likely to get back on track faster than those who don't. So we'll continue to work with lenders to raise awareness of our Hardship Solutions program, and in the process help borrowers not only stay in their homes, but improve overall consumer confidence at the same time.

There is much more to be found in this edition of **Streets Ahead**. We hope you find it a useful report which helps you better understand changing consumer sentiment in the mortgage market.

Warm regards

Ellie Comerford
Chief Executive Officer
Genworth Financial

Executive Summary

Welcome to the second edition of **Streets Ahead** and the results of the Genworth Homebuyer Confidence Index (Genworth HCI) for March 2011. The report and biannual index detail current and historical confidence levels among Australian homebuyers and aspiring borrowers based on surveys of more than 13,000 Australians between 2005 and 2011.

National disasters tip confidence

In the 2010 Index released in September last year, we found homebuyer confidence was on a delicate balance as borrowers remained cautious about rising interest rates and higher costs of living. The March 2011 Index, based on a survey of consumers conducted in February, finds the recent devastating natural disasters have weighed heavily on confidence. Growing debt discomfort and higher incidences of mortgage stress in affected states have caused the Index to fall by 1.5% from 2010 levels. Indeed, national homebuyer sentiment would have increased by 0.8% if it wasn't for the drop in consumer sentiment in Queensland; the state most affected by events of the past summer.

Genworth's hardship data, which helps paint a clearer picture of borrower distress, tells a similar story. Total hardship requests increased by over 70% in 2011 (to mid-March) compared to the same period last year. Nearly half (40%) of these requests were natural disaster-related, mainly driven by the flooding in Queensland.

A telling trend from the survey showed that one in five (21%) respondents affected by the flooding in Queensland believed it would take them more than six months to get back on their feet, beyond the standard three month hardship solutions currently offered by many lenders.

Queensland and Western Australia the most fragile

It's not just flooding, cyclones and bushfires that are impacting the country's resources states. Other data shows house prices are declining across Queensland and Western Australia after years of strong economic growth. Residents of these states are not only showing greater pessimism about the housing market than the rest of the country, but are also experiencing greater difficulty servicing their debt. In fact, 9% of Western Australia residents surveyed said they had trouble making their debt repayments every month, compared to the national average of just 3%.

Higher cost of living adds to borrower hardship

The rising cost of living, in particular higher food prices, has become the main concern for borrowers expecting difficulty meeting mortgage repayments. This has overtaken concern over interest rates rises, which most troubled borrowers in 2010.

First homebuyers are upbeat but the year ahead will be the real test

After some concern first homebuyers (FHBs) over-committed in the bid to take advantage of the government incentives in 2008 and 2009, **Streets Ahead** finds these borrowers are faring well. They're more confident than the average, are less likely to have experienced mortgage stress and are also more comfortable with higher debt levels. But the year ahead could be crunch time, with nearly one in four FHBs expecting to find it hard to meet their mortgage commitments.

By tracking over 13,000 Australians the Genworth HCI is an invaluable measure of the sentiments of mortgage holders

About the Genworth Homebuyer Confidence Index

Market trends and borrower sentiment are keenly sought after in today's mortgage and property market—a market which underpins Australia's continued economic prosperity. From 2005–09 Genworth addressed this demand with the annual Genworth Financial Mortgage Trends Report, providing a comprehensive overview of the changing attitudes of Australians to the mortgage and property market.

In 2010, Genworth first used the data collected from surveys conducted between 2005 and 2010, in combination with its own unique data built up over more than 45 years, to devise an index which tracks important changes in sentiment within the mortgage and property market. This report is the March 2011 edition of the Genworth HCI and draws from our data, collected from over 13,000 Australians, to provide useful trends in homebuyer confidence.

The components used to create the Genworth HCI are:

1. Proportion of monthly income currently used to service debts
2. Maximum loan-to-value ratio (LVR) comfortable in borrowing
3. Last 12 months repayment history
4. Next 12 months repayment history
5. Whether it is a good time to buy a home.

The Genworth HCI is released biannually in March and September.

2010–11: Natural disasters take their toll on sentiment

After remaining stable throughout 2009-10 the Genworth HCI fell 1.5% in early 2011 from 99.1 to 97.6. Despite Australia's relatively strong economic performance over the past few years, the Genworth HCI has not reached the highs seen in 2007 and has now seen two consecutive decreases since 2009.

While many major economic indicators including unemployment and GDP remain strong, official and lender interest rate rises in late 2010 placed further strain on many households. However, by far the biggest contribution to the fall in confidence in early 2011 is the spate of recent natural disasters, most notably Cyclone Yasi, the floods in Queensland, northern New South Wales and Victoria, as well as bushfires in Western Australia.

Queensland borrowers the worst affected

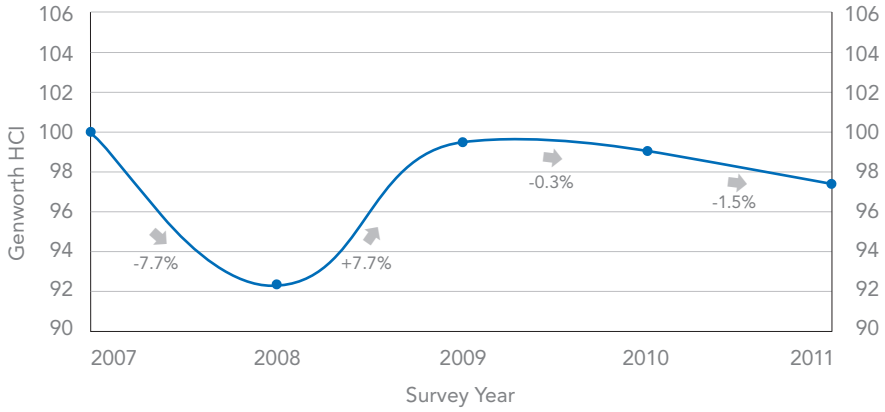
Taking a closer look at borrower experiences in these affected areas, the survey found one in three Queensland respondents (33%) were affected by natural disasters in some way, compared to the national average of 14%. A further 16% of Victorian respondents stated they had been affected, compared to just 9% in New South Wales.

Genworth hardship data also shows the disasters have hit Queensland hardest, with (at the time of printing this report) 91% of all disaster-related hardship applications coming from Queenslanders.

The incidence of natural disasters in the state has shaken Queensland homebuyer confidence. One in four (25%) surveyed

Genworth Homebuyer Confidence Index

Source: Genworth Financial



One in three

Queensland respondents were affected by natural disasters in some way

Recent disasters

…some 45% of affected households are looking to take on more debt to aid their recovery

feel negatively about the outlook for the property market over the coming year, compared to the national average of 19%. Demand for property in flood and cyclone affected areas seems likely to drop, with 16% of those affected by the natural disasters planning to move to safer ground. Extensive media coverage of disasters is also likely to affect tourism in and migration to these regions.

The difference in sentiment in Queensland alone is such that if the Queensland data were excluded from the Genworth HCI, the Index would have increased in 2011 to 99.9. This emphasises the extent of the impact of recent natural disasters on the state's residents.

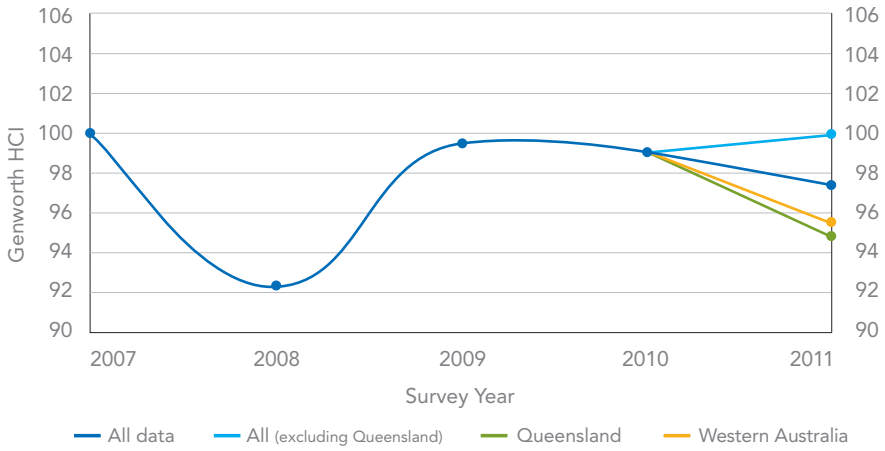
While the immediate impact on confidence is stark, most of those affected by recent natural disasters were fairly optimistic about their recovery, with 60% expecting to recover in two months or less. One in five (21%) believed they would be affected for more than six months, an indicator that there is a need for the industry to develop longer-term hardship solutions beyond the standard three months offered by most lenders.

With workplaces, food costs, transportation and housing all affected by floods, many households are likely to face considerable strain. Some 45% of affected households are looking to take on more debt to aid their recovery. With property and job security in some industries affected, many Queensland borrowers are likely to face even greater difficulties servicing their mortgage and any additional debt. As this survey was conducted in February 2011, more borrowers are likely to feel the effects of floods on their repayment abilities in the months to come.

The Genworth HCI would look very different without Queensland and Western Australia's fall in confidence

Queensland and Western Australia have dampened homebuyer sentiment in early 2011. The confidence index in Queensland fell to 94.8 in 2011, while Western Australia was slightly higher at 95.6. In the past, these two states have benefitted from the mining boom but sluggish house price growth in 2011 and natural disasters have affected confidence.

Source: Genworth Financial



Western Australia also suffers from falling sentiment

Looking at future expectations for property markets in the worst disaster affected regions, Western Australia residents were the most pessimistic about the property market in the coming year, closely followed by Queensland residents. This drop in homebuyer sentiment is not unwarranted, with Queensland and Western Australia being the only states to see house price declines in their capital cities in the December 2010 quarter, according to the Housing Institute of Australia (HIA).

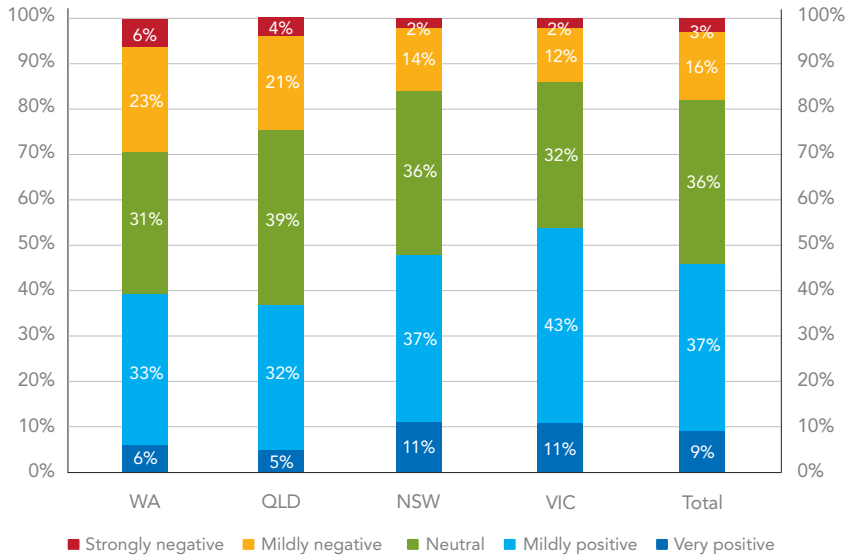
Similarly, Western Australia and Queensland borrowers were more likely to be struggling with mortgage repayments, with 9% of Western Australia borrowers having difficulty making repayments every month over the past year, compared to the national average of 3%. Queensland borrowers also struggled, with 5% having difficulties making repayments every month over the past year and 21% having difficulty in some months, compared to the national average of 18%.

Significant affordability and repayment concerns, combined with continuing uncertainty about the mining tax and the aftermath of recent flooding, bushfires and Cyclone Yasi means that Western Australia and Queensland housing market sentiment is likely to continue to be subdued in 2011.

Do you feel positive or negative about how the Australian property market will perform over the next 12 months?

Western Australia and Queensland sentiment has been affected by falling prices and increases in arrears. Western Australia had the highest proportion of residents who felt negatively about the property market, and Queensland had the lowest proportion who felt positively about it.

Source: Mortgage Trends Survey, analysis conducted by RFi



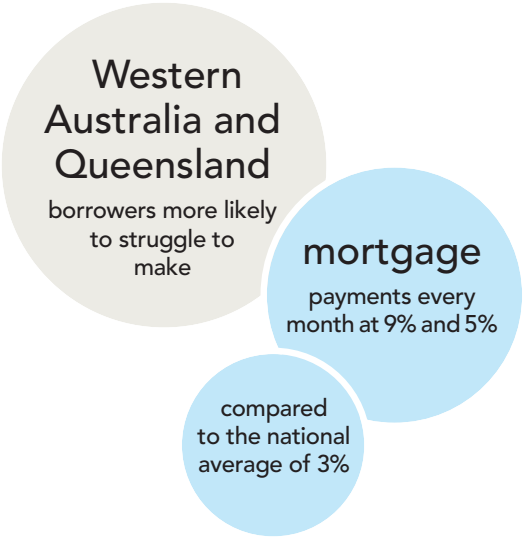
More are aware of Government relief than lender hardship programs

As the extent of the damage in Queensland from the floods emerged, the state and federal governments announced financial and hardship assistance for those affected. **Streets Ahead** found awareness of these government initiatives was high. Almost four in five (78%) respondents nationwide, including 92% of people whose homes had been damaged or destroyed by natural disasters, were aware of government relief programs.

Many lenders and insurers augmented government initiatives by providing their own measures to help affected borrowers. Borrower awareness of these lender-provided hardship solutions was lower at 39%, with 14% of those who were aware having used them in the past. Those affected by the floods were more likely to be aware of lenders' hardship solutions, with 46% aware of them and 18% having used them in the past.

Generally, using a lender's hardship solutions service was a positive experience, with 61% satisfied with the service and only 22% dissatisfied. While some borrowers questioned the long-term impact of the relief many said it had helped them through a tough time.

Genworth has approved over 1000 hardship requests to those affected by natural disasters so far in 2011 (to mid-March), with weather events behind a 70% increase in total hardship requests during this period (compared to the same period in 2010). The majority (91%) of these natural disaster-related requests were from Queensland, with northern New South Wales and Victoria among other affected areas. Almost all (96%) of the claims were due to floods, rather than bushfires or Cyclone Yasi.



Growing discomfort despite unchanged debt levels

Turning back to trends across the nation, household debt levels did not change during the period, with 27% of respondents in both 2010 and 2011 surveys putting half or more of their monthly income to paying off debt. However, households have become more conservative about how much debt they are willing to take on, with the proportion willing to borrow more than 80% of a property's value falling 10% from 39% to 29%. This suggests that other factors such as the rising cost of living are causing borrower concern.

Queensland residents have a larger debt burden than other Australians, with one in three using more than half their income to service debt. Although the level of debt is increasing for Queensland and Western Australia, these residents are only marginally less comfortable in borrowing larger amounts.

Mortgage stress up, but borrowers remain optimistic

Though household debt levels have remained constant, the rising cost of living and the effects of natural disasters have led to a greater degree of borrower stress with 21% of borrowers finding it difficult to meet their mortgage repayments in the 2011 survey, up from 15% in September 2010. This increased stress sees borrowers less willing to become more leveraged or invest in new property.

Unsurprisingly, Queensland and Western Australia residents were more likely to have experienced trouble making repayments, with Western Australia residents having the highest proportion of borrowers who experienced trouble meeting repayments in every month.

Despite past strain, borrowers remain fairly optimistic about their ability to meet repayments over the coming year, perhaps due to the expectation interest rates will remain unchanged in the short-term.

1 in 3 Queensland
residents are using more than half their income to service debt

Western Australia
has the highest proportion of borrowers experiencing trouble meeting repayments

2011 a better time to buy a home

Pushing up the Index was an increase in the proportion of respondents who believed now is a good time to buy a home (up from 25% to 38% in March 2011). This was the only positive movement in the Index over this six month period, and the only area in which Queensland and Western Australia residents were more optimistic than others. In fact, 40% of Queenslanders and 49% of Western Australians believe now is a good time to buy a home, compared to the national average of 38%.

Households are more

conservative with fewer choosing to borrow more than 80% of a property's value

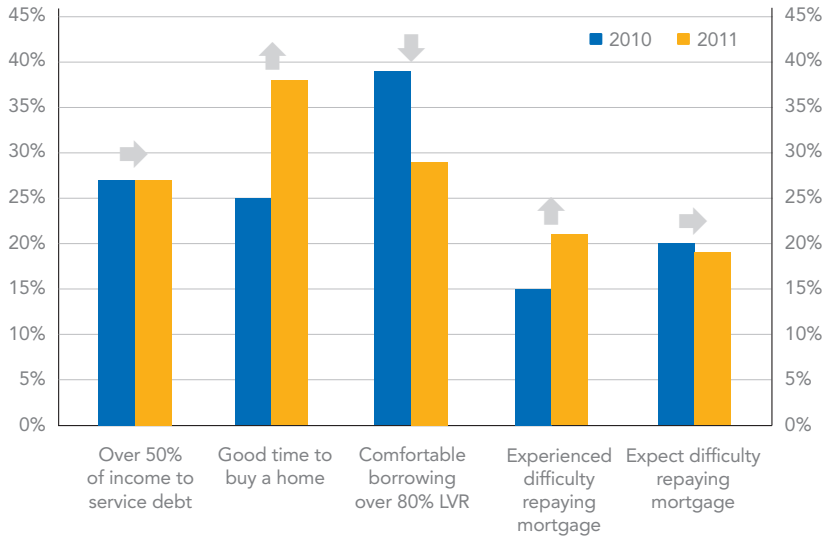
Despite

past strain, borrowers remain optimistic with an expectation that interest rates won't rise

Index factors—change

'Good time to buy' was the only index factor to see a positive change between the past two surveys, with household debt levels and expectation of mortgage stress remaining unchanged. The fall in the index was driven by an increase in experience of mortgage stress and decreased comfort with higher debt levels.

Source: Mortgage Trends Survey, analysis conducted by RFi, 2010 survey conducted by UMR



First homebuyers more confident overall but pessimistic about future

Overall, FHBs—those that have purchased their first home in the last 12 months or are looking to purchase their first home in the next 12 months—are more confident than the average homebuyer.

Despite concerns by some that FHBs may have entered the property market too early in order to take advantage of government incentives offered during 2008 and 2009, **Streets Ahead** finds indebted FHBs were slightly less likely to have experienced stress in the past year at 17% compared to the average of 21%.

FHBs are also more comfortable with higher debt levels. Almost two in five (38%) are comfortable taking on an LVR of more than 80%, compared to the average of 29%. This is likely due to strong house price appreciation making high LVRs inevitable if FHBs are to realise their dream of home ownership.

But it's not all good news for this segment. Nearly one in four (24%) expect to find it difficult to meet repayments over the next 12 months compared to the national average of 19%. This pessimism is largely fuelled by the threat of further rate rises, in contrast to the average borrower who was most likely to be concerned by the rising cost of living. Interest rates are likely to be of greater concern to FHBs because they are more heavily geared, with one in three spending more than half their monthly income on servicing debt, compared to the national average of 27%.

Cost of living overtakes interest rate rises as top concern for strugglers

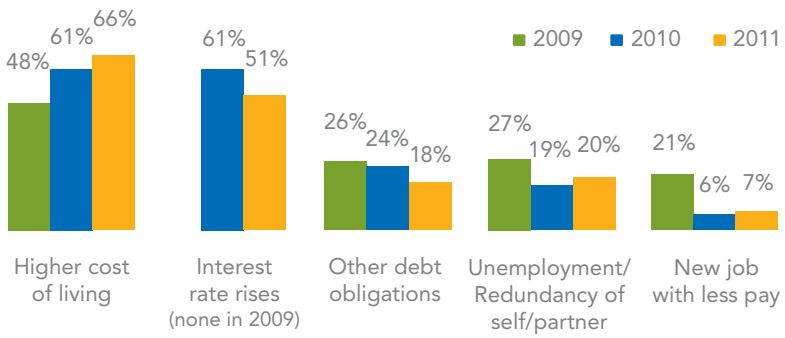
Nationally, the proportion of borrowers expecting to have difficulty meeting repayments over the coming year has held steady since 2010 at 19%. However, while interest rates have risen and are expected to rise further, more borrowers expecting to struggle to meet repayments cite the rising cost of living rather than rising rates as the key problem, at 66% compared to 51%.

Future repayment difficulties

The higher cost of living has overtaken interest rate rises as the number one concern for those expecting to face problems meeting mortgage repayments.

Source: Genworth Financial

Why will you find it difficult to meet your mortgage repayments in some/all months?



First homebuyers

are more confident than the average homebuyer and are more comfortable with higher debt levels

Confidence

should be returning among borrowers but natural disasters are likely to weigh on sentiment

The higher cost of living is driven by factors including the higher cost of energy exacerbated by unrest in the Middle East, and the rising food prices resulting from widespread flooding in Queensland. Between September and December 2010 the greatest increase in the Consumer Price Index was on food, increasing 2.2% over the quarter, which is likely to have a noticeable impact on all households and on consumer confidence generally. Electricity and other utility prices are expected to increase further across the country, with utility prices having increased around $1000 a year in Western Australia, and privatisation expected to put upward pressure on energy prices in New South Wales.

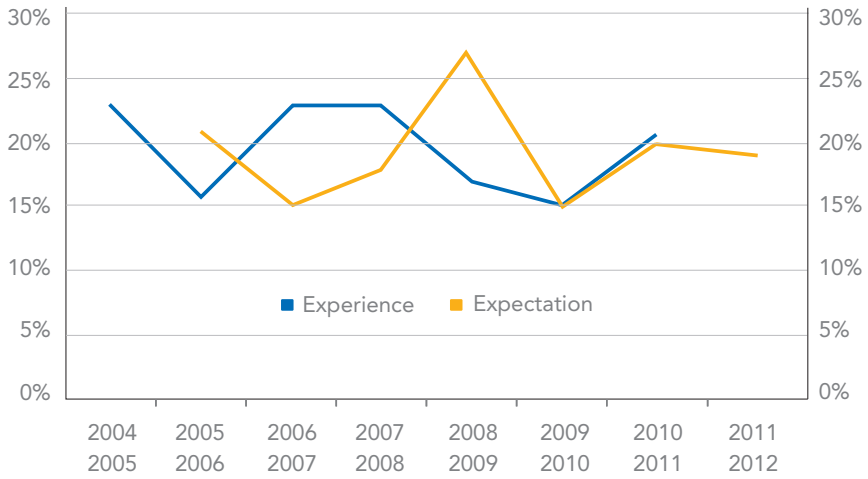
Hardship expectations reflect reality; outlook continues to be subdued

For the first time since the Index began, **Streets Ahead** finds expectations of hardship were almost in-step with actual experiences in 2010–11, suggesting confidence should be returning among borrowers. Indeed, at a national level homebuyer sentiment has been fairly strong and were it not for the Queensland floods the Genworth HCI would have ticked up in early 2011. However, the effects of the natural disasters are likely to be a continuing weight on sentiment in the coming year with a further decline predicted in the second half of 2011.

Expectation vs experience of hardship

The proportion of mortgage holders who expected hardship in the 12 months following a survey are compared to the proportion who actually experienced hardship in the 12 months prior to the subsequent survey—effectively providing a comparison over the same period of time.

Source: Genworth Financial



The lenders' perspective

2010 was a tough year for most lenders in the mortgage industry as the rising cost of funding and weaker consumer demand adversely affected the housing market. FHB demand was also weak following the withdrawal of government stimulus while investor activity remained subdued. In early 2011, the focus for growth has shifted to refinancers, with several larger players investing in substantial advertising to attract customers from their competitors.

Lenders are now also re-entering the high LVR segment of the market in a bid to grow their lending books. This trend was flagged by lenders in Genworth's **Home Grown:** Mortgage Industry Perspectives report last November as a key strategy to gain market share and address continuing affordability concerns.

The economic backdrop

Unemployment continued to fall from its peak of 5.8% in August 2009, reaching 5.0% in December 2010. While unemployment and interest rates have become less of a concern to borrowers, the rising costs of food, petrol and housing are placing a strain on households.

Meanwhile, interest rates rose 25 basis points in November 2010, and many economists expect the RBA to leave rates unchanged for the short-term while consumer sentiment and retail spending continue to be subdued. That being said, rate increases are predicted for mid to late 2011. The expected moderate interest rate rises this year should contribute to a stabilisation in housing affordability.

Economic Indicators

Sources: ABS, RBA, HIA, NYMEX

Economic indicators*	2007	2008	2009	2010	2011
Official cash rate	6.25%	7.25%	3.00%	4.50%	4.75%
Inflation	2.4%	4.5%	2.5%	3.1%	2.7%
Unemployment	4.3%	4.3%	5.8%	5.1%	5.0%
Oil prices per barrel US$	$66.30	$127.76	$67.73	$75.69	$96.97
HIA Housing Affordability Index	100.0	92.4	69.5	69.5	53.5
Average FHB loan	$238,600	$243,100	$270,200	$283,300	$280,800

*As at June of each year, in 2011 figures are as at February 2011, or the most recent available at the time of writing

Flooding, fires, cyclones, and moderating house prices have weighed heavily on Queensland and Western Australia's residents

As the cost of living increases and interest rates rise, Australians have become more conservative in their borrowing

Yet more of us believe now is a good time to buy a property

Conclusion

Conditions over 2010–11 have so far been mixed with positive economic data undercut by the effects of several natural disasters, particularly the Queensland flooding. This has resulted in homebuyer confidence dipping slightly for the second consecutive period. Had it not been for these disasters, the Genworth HCI would have increased in the March 2011 edition.

While flooding, cyclones and bushfires combined with moderating house prices in Queensland and Western Australia weighed heavily on residents in these states, their steely determination is reflected in their optimism with most expecting to bounce back in two months or less. The focus will be on managing additional debt burdens, with almost half of affected Queensland households looking to take on more debt to aid their recovery.

It's pleasing to see most of those affected are aware of government support and of those aware of lender initiatives, most were happy with the service. Still, more needs to be done to help the one in five expecting longer-term hardship as a result of natural disasters.

During the past three months Genworth has helped over 1000 disaster-affected borrowers by working with lenders to offer hardship relief. However, all borrowers experiencing hardship need to be encouraged to contact their lender as soon as difficulties arise, as early action is essential to a fast recovery.

For the rest of the country, expectations for a stable interest rate environment and soaring food and petrol prices has meant the rising cost of living now tops the list of consumer concerns. As a result, Australians are becoming more conservative in their borrowing. This is despite more of us believing now is a good time to buy a property.

First homebuyers have fared well despite the higher cost of living and rising interest rates. There was some concern this segment may have over committed in the rush to take advantage of government incentives in 2008 and 2009. We will continue to watch this FHBs group closely as nearly one in four (24%) expect to face problems in the year ahead.

genworth.com.au/streetsahead

About Genworth

Genworth Financial (Genworth) is a leading provider of lenders mortgage insurance (LMI) in Australia and New Zealand. In partnership with lenders, our aim is to make home ownership more accessible to borrowers through provision of LMI solutions.

Working with close to 200 lenders, Genworth has built a reputation for its expertise in understanding the evolving mortgage market. Our financial strength is underpinned by our A$3 billion investment portfolio, and our rich data gained through insuring mortgages for over 45 years.

Our Hardship Solutions team was formed in 2006 and, in conjunction with lenders, has assisted over 18,000 (as at Q4 2010) borrowers to stay in their own homes.

For more information visit genworth.com.au

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About RFi

RFi is a strategic research business that delivers research and analysis by identifying and formulating projects within the arena of retail finance. RFi's business model is underpinned by B2B and B2C primary research, a factor which enables RFi to determine the key issues affecting any market.

For more information visit rfintelligence.com.au

Home Grown: Mortgage Industry Perspectives

Home Grown, Genworth's biannual report exploring borrower and would-be borrower sentiment. The November 2010 edition is now available. **Find out more at genworth.com.au/homegrown**

Disclaimer

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