



RMBS plays part in Australian economic recovery

By Kim Cannon**, 19 August 2009

While the banking system, and the 'Big Four' banks specifically, gets most of the attention in terms of the part played by the financial sector in the Australian economy's emerging Global Financial Crisis (GFC) resilience story, the Federal Government's scheme via the AOFM to support the non-bank residential mortgage sector cannot be underestimated.

The Federal Government has injected \$4 billion of secured funds in AAA rated Residential Mortgage Backed Securities (RMBS) tranches issued by the non-bank lending sector over the past 12 months as part of its scheme to maintain competition.

This has played a strong part in stabilising the country's residential property market, maintaining confidence in the non-bank financial sector and ensuring consumer choice as the recovery takes hold – in contrast to the panic and pandemonium in the United States.

While the current downturn in the Australian economy has resulted in a concentration of market power with the Big Four banks where almost 90 per cent of all residential home loans are now held, the "other lender" category has not only survived but is now itself also seeing a pick-up in activity. It is in the interests of all consumers for a robust and multi-tiered banking system to exist. There are currently several participants in the non-bank sector, but how long will this be the case?

The recent purchase by NAB of Challenger's mortgage management division is a timely reminder of the opportunities which the current economic cycle will provide the Big Four banks with to further concentrate lending in Australia.

While the Australian economy seems to have weathered the worst of the initial GFC shock the risk to consumer choice and competition in sectors like property lending are real and potent for home owners and investors.

The non-bank securitisers provide critical competition to the Big Four banks and were largely responsible for the historic reduction in home loan margins following the banking deregulation of the 1980's.

As an example of how the Federal Government's scheme has worked, through tender processes running since November 2008, FirstMac secured \$1.2 billion of Residential Mortgage Backed Security (RMBS) investment in two tranches, with the Australian Office of Financial Management (AOFM) providing a cornerstone investment of \$1 billion and an additional \$200 million being raised by FirstMac from external investors. The investments, which were rated AAA by two rating agencies, were made in prime residential mortgages to borrowers with no credit default history, fully mortgage insured, and with an average loan to value ratio of 71%.

There are four major non-bank providers of prime residential mortgages in Australia and all four have received mandates from the AOFM, of which three, including FirstMac, have received two mandates.

The Federal Government's thinking is that this type of investment in RMBS would pass through to home buyers and investors in an effort to support the residential lending sector.

FirstMac was able to significantly increase new lending volumes as a consequence of these successful transactions specifically through the release of a new product range called "FightBack". Since the first investment \$880 million of loan applications have been taken with daily volumes continuing to climb.



The Government's objective in directing the AOFM to invest in RMBS was to support competition in lending for housing from second tier lenders, such as FirstMac. This support means that Australia will emerge from the GFC with more than just the Big Four banks still standing. This is positive for consumers.

In tandem with the bank deposit guarantee, the injection of spending via the two major stimulus packages and the rapid reduction of interest rates by the Reserve Bank to near-record lows, the RMBS scheme has ensured that an important sector outside the Big Four has continued to provide loans to people who prefer to have a choice of lender.

FirstMac has seen steady demand through the 2008-09 financial year and a marked increase in loans over the past three months.

This is a strong indication that the RMBS scheme has been a success for the Government as one of the key thrusts of its GFC-resistant defence.

Participants in this sector are committed to providing a competitive and quality alternative to traditional banks in the residential mortgage sector.

Continued Government support in the form of the existing AOFM scheme until we see a recovery in the wholesale markets is critical. A second round of AOFM RMBS investment will satisfy the Government's requirement of being timely, targeted, and temporary. This is clearly a superior approach to the alternative of government guaranteed RMBS as the market difficulties relate to liquidity not credit.

****Kim Cannon, Managing Director of FirstMac, founded FirstMac Limited as a mortgage manager and originator of loans to various third party funding programs in 1988. While a "silent achiever" in the industry, Kim has played an integral role in the growth and development of the non-bank lending market in Australia over the past two decades. During this time, he has assembled an enormous bank of knowledge and street smarts about the industry and business. Kim was a key figure in the early formation of the Mortgage Industry Association of Australia, now known as the MFAA. He has also been instrumental in enhancing many of the industry products, including developing the first non-bank loan for residential construction and blended loans, while bringing much-needed competition to the finance sector. Kim has continued to develop the business and create a real point of different to other lenders by embracing new technology, and offering superior innovative service and systems.**

About FirstMac Limited

FirstMac Limited is a leading Australian owned mortgage finance lender with almost 30 years experience. It delivers a comprehensive range of loan funding, loan servicing and portfolio management services. FirstMac initially originated and managed home loans through major third party providers, but in 2002 entered the securitisation market and began self-funding its own loan business, by issuing AAA-rated bonds on global capital markets.

FirstMac's presence has grown through the provision of wholesale funding via a national distribution network of mortgage originators and brokers. FirstMac has an 'Above Average' Standard & Poor's servicer rating.

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