Australia's housing 'co-ops' foresee bright future

By Cameron Algie

AUSTRALIA's co-operative housing societies, which are wholly mutual, member orientated financial institutions, have experienced a 500% upsurge in lending in the last five years to the point where they were directly lending or servicing in excess of $1.67 billion in 1988/89.

This is a remarkable situation, bearing in mind that previously many people believed that the role of the co-operative housing society as a non-deposit taking institution for housing had finished. Current lending results would appear to indicate an extremely bright new era for this old financial institution.

Co-operative housing societies, initially formed in Britain in the late 1800s, became the basis for the modern permanent building society in Australia. The majority of co-operative housing societies were formed in Australia shortly after the second world war to provide access to housing finance to the many returned servicemen and low and middle income earners who traditionally could not gain access through the major trading banks and other lending institutions.

In New South Wales, from 1937, and in the other States, from 1945, they became dominant lenders of housing finance in the '40s and '50s. In the 1950s they became the major agents of State Governments in providing home purchase assistance funds to the community. Since inception in Australia they have lent in excess of $7 billion for housing.

The development of the savings bank system in Australia in the 1950s and the permanent building societies in the 1960s led to the belief that the role of a co-operative society as a major provider of housing finance had ceased. Their primary dependênce upon other institutions had made them vulnerable to the supply of finance.

As a result of the decline in activity in the 1970s, societies throughout Australia were lending only $316 million in 1984/85, or 2.7% of all finance for owner-occupier homes in Australia. In 1988/89 this had risen dramatically to $1.672 billion or 9.5% of the residential home loan market — an increase in volume of over 530%.

Major sources of funding over this period have changed to represent the new retail agency role of societies for the secondary mortgage market. Sources were:

The rise in co-operative lending for housing finance can be attributed to the changing dynamics in the Australian financial system caused largely by deregulation of the financial sector, the 1987 share market crash, the developing secondary mortgage market and the development of specialist lending roles for financial institutions.

The growth of society lending is also interesting as they are non-capitalised financial institutions and depend upon their funding sources emanating from other financial institutions. Growth of funding from the banking institutions is particularly important. In the State of Victoria, for example, the Government-owned State Bank of Victoria has lent in excess of $500 million since 1985. Other major banks, including the Commonwealth Bank, Westpac Bank and the ANZ Bank, have also utilised the specialist agency role of societies.

	1984/85 $	1988/89 $
Government	—	124,000,000
Insurance Companies	350,000	—
Banks	89,716,000	383,431,675
Other	300,000	—
Secondary Mortgage Market	—	115,000,000

The only States not to share in this upsurge in lending are Queensland, which is suffering from legislative restrictions preventing an expansion of its activity, and South Australia, which, until 1988, had not formed the modern co-operative housing society.

Perhaps the most significant development has been the expansion of the secondary mortgage market, particularly where governments had initiated schemes through that sector for the purposes of supplementing their existing housing

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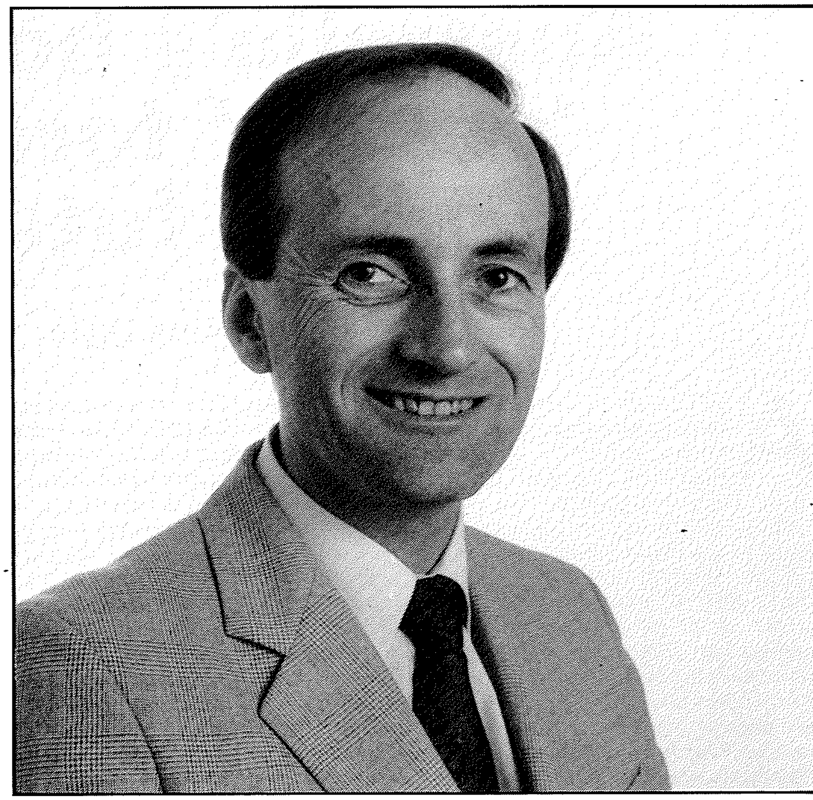
assistance programmes. It is in the provision of a retail agency network with low cost administration and lending expertise that societies have played a most significant role. In 1987/88 only $188 million was provided in New South Wales under their Premier Low Start Loans Scheme and in 1988/89 $1 billion was provided in that State, and the recently formed Home Opportunity Loans Scheme in Victoria provided an additional $115 million through Societies.

Societies present a network of over 250 offices throughout Australia and the recently formed co-operative housing society in South Australia will complete this network.

Another feature leading to their success is that societies are not deposit takers. Their legislation excludes this feature. It is this factor that enables them to act as a truly independent agent on behalf of other lending institutions. Societies introduce reciprocal commercial and borrower business to major institutions if this is required, and therefore do not act in competition but rather in a complementary role, expanding market share for the primary institution.

Societies have a low operational cost, operating at margins between 0.6% and 0.8% of an interest rate equivalent compared to the major institutions' operating costs of between 0.25% and 0.35%. Societies are able to use their non-profit, wholly mutual structure to discount interest rates received on a wholesale basis. They also use their member reserves to pass on the benefits of wholesaling to reduce interest rates by between 1% and 1.5% below the general housing interest rate.

Societies have a specialised constitutional role and can only lend on owner-occupied residential mortgages. They lend on high loan to valuation ratios — usually up to 95% — and, if the lender requires, have access to State Government guarantees and indemnities. Guarantees are made available if they meet the



Government's criterion, which is basically that the funds raised are between 0.5% and 0.75% below the general housing interest rate.

Over societies' history, claims on Government guarantees and indemnities have been minimal — in the vicinity of 0.009%. Where funds are not guaranteed they are lent with mortgage guarantee insurance when the loan usually exceeds 80% of the valuation. Societies' record of claims experience under this form of insurance is also excellent, maintaining a high reputation with the major insurers in Australia — HLIC and MGICA.

Given their recent performance, the outlook for societies remains extremely bright. Continued deregulation of the financial sector and the need for the Australian economy to compete on a national scene will increase competition and therefore specialisation of financial roles within Australia. Societies' low cost and profit-sharing philosophy and their capacity to benefit from the wholesaling of funds while maintaining market shares for major institutions places them in an excellent position to play a dynamic role for the future.

Finally, the development of the secondary mortgage market in Australia, which to date has taken a different role to that of the market in the United States and other countries, will further utilise the societies' role to act as a retail agent to service this sector.

Societies' future is one where both private institutions and governments will continue to look favourably upon the use of the unique co-operative retail agency. ■

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