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Views sought on debt servicing restrictions framework

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The Reserve Bank of New Zealand – Te Pūtea Matua – is seeking feedback on the merits and design features of debt serviceability restrictions (DSRs) on residential mortgage lending.

“We are not proposing to implement debt serviceability restrictions at this time, but we want to prepare for implementing them in case financial stability risks warrant it,” Deputy Governor Geoff Bascand says.

We use macroprudential tools to reduce the financial stability risks associated with ‘boom-bust’ cycles in the economy. This in turn helps us to meet our statutory purpose of ‘promoting the maintenance of a sound and efficient financial system’. Our most commonly used macroprudential tool is loan-to-value ratio (LVR) restrictions. These measure how much a bank lends against mortgaged property, compared to the value of that property.

We are seeking feedback on the merits and potential design of two types of DSRs: restrictions on debt-to-income (DTI) ratios – which impose a cap on debt as a multiple of income; and a floor on the test interest rates used by banks in their serviceability assessments which test the ability of borrowers to continue repaying their loans if interest rates rise to a certain level.

“Although the financial system remains strong and banks are well-capitalised, we are concerned that the combination of very high debt levels and unsustainable house prices poses financial stability risks, particularly if current high-risk lending flows remain unchecked. Adding more options to our macroprudential toolkit will help us to address these risks if needed,” Mr Bascand says.

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Our initial assessment indicates that DTI restrictions are likely to be more effective than test rate floors in supporting financial stability and sustainable house prices. DTI limits link credit availability to income growth and can therefore be more effective in constraining debt levels over a longer period compared to other macroprudential tools. DTI restrictions are likely to take six to nine months to implement, while interest rate floors could be deployed faster, making them a useful interim measure.

DTI restrictions can also be calibrated to minimise impacts on first-home buyers. This would align with the formal direction issued to us by the Minister of Finance and with our Memorandum of Understanding on macroprudential policy.

We invite feedback from interested parties until 5:00pm on 28 February 2022.

More information

- Consultation Papaer: Debt serviceability restrictions
- Housing matters for financial stability risks, November 2021
- Reserve Bank tightens LVR restrictions, September 2021
- Debt serviceability restrictions added to policy toolkit, June 2021

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