

Radical thinking

The cosy world of Australian home lending could be in for a big change if an innovative new way to spread risk and reward takes hold, writes **Ben Wilmot**.

A radical equity finance mortgage scheme now being marketed to institutions could slice the cost of a mortgage.

A venture between Rismark International and Macquarie Bank aims to raise \$1 billion from superannuation funds to create a pool of money to invest in equity finance mortgages.

The products promise to cut the cost of deposits and, most importantly, monthly payments, in return for an interest in a home's capital appreciation.

While the fund's raising is in the hands of superannuation funds and the consultants, who act as gate keepers for the industry, the idea has captured public attention.

Zelda*, a 46-year-old public servant who rents in Sydney's inner western suburb of Ashfield, says she is waiting with bated breath for the launch of a housing equity finance scheme.

Although she has been saving, "ridiculously high" home prices have meant her savings can't match the deposit required, and she needs the assistance of investors to fund her home purchase.

"I would very much like to participate so I can eventually afford to own my first home," she says.

Zelda was quick to spot the broader implications for the housing market. "I got excited reading the [Prime Minister's Home Ownership] taskforce's findings and strongly believe that the recommendations if implemented will have tremendous impact on the property market," she says.

Rismark executive director Richard Facioni says that housing affordability is at an absolute low point and this is what equity finance mortgages are designed to address.

"They promise to cut the cost of deposits and payments."

Interestingly, Facioni says that first-home buyers make up only 15 per cent of annual mortgage issuance, and Rismark's product would just as likely appeal to people who already have a property and want to guard against a change in circumstances.

James*, a "simple geologist" living in Mosman Park near Perth, has a different story. He is a home owner who wants to refinance using an equity finance mortgage. He says this prospect is

"very important" for his growing family as it will free up capital for him to live on.

Liberal MP Malcolm Turnbull, a supporter of the idea since its inception as a Menzies Research Centre paper, says the concept has a number of potential applications. "It does have the potential to make housing more affordable . . . it also has some advantages at the other end of the spectrum," he says.

"The ability for people who are older . . . the empty nesters who have paid their mortgage to realise some of the value in their home without taking on additional debt."

For Louis Christopher, research director at Australian Property Monitors, the most interesting question raised by Rismark's proposed equity finance mortgages is the question of whether the masses will take them up or not. "That's the million dollar question," he says.

He says that if the product succeeds in the mass market, it could influence house prices.

"It enables people to borrow money that they otherwise wouldn't be able to borrow," he says. "It increases the buying power of house buyers."

to shake up the mortgage market

"Do they use their new equity power to reduce the loan on a \$500,000 home or do they instead decide to buy an \$800,000 or \$900,000 home?" Christopher asks.

With choices like this, the analyst is upbeat on Rismark's prospects.

"I think the odds are this thing will take off," Christopher says.

One of Australia's foremost finance academics, New York University Stern School of Business professor of finance Stephen Brown, who served on the home ownership taskforce, which fleshed out the equity finance mortgage concept, is enthusiastic about Rismark's plans.

Brown says the Australian banking industry is known for a general lack of innovation and the chief virtue of Rismark's product is that it will breach the barriers that have so far protected the nice and cozy world of Australian housing mortgages.

Facioni is at pains to emphasise that equity finance mortgages are complementary to banks' existing product suites, and Rismark is not trying to replace traditional mortgages, but if the innovation catches it could transform the way consumers deal with their banks. Rather than being subservient to debt lenders, they will be able to access equity from a source that could tip the scales more in their favour.

From the point of view of an individual's finances, Brown says that in the present heated real estate market, the average Australian is taking an inappropriate risk position by investing so much of their wealth into the one, undiversified asset represented by their house.

"This plan allows average people the opportunity of shouldering off the heavy risk and return of this housing asset to those who are willing, and indeed eager to take it on," Brown says.

Brown, who has been in the US for several decades, says that equity participation mortgages were actually quite popular in

"If this succeeds, it will be the mouse that roared."

that country in the late 1980's, but they failed.

But he says the securitisation of the mortgages being proposed by Rismark is something new.

Brown says that equity participation mortgages failed because of a weakness in American contract law that doomed the contracts. In the US, when the properties rose in value, home owners were naturally unwilling to share their good fortune with banks. By the same token, if houses

fell in value, then banks would accuse owners of not having maintained the property. These disputes were mired in litigation, which meant that US banks ran away from the mortgages.

However, Rismark says that under Australian contract law its mortgages are iron clad.

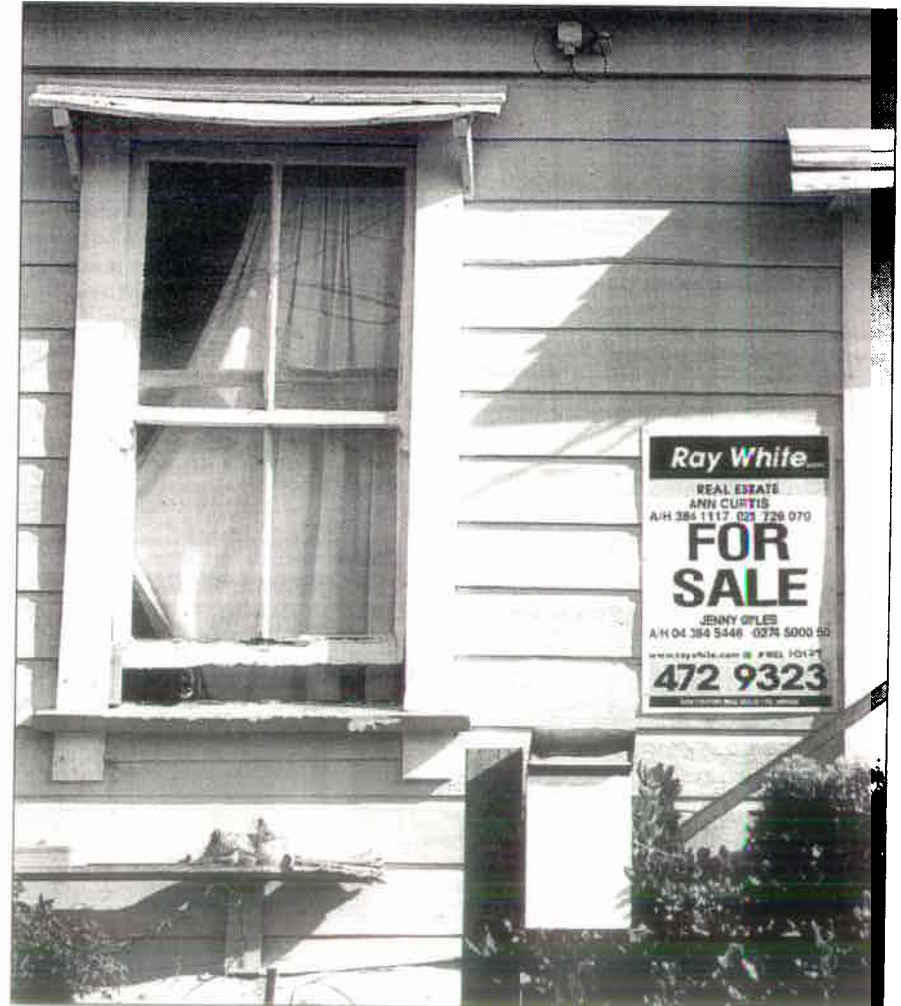
"If this succeeds, it will be the mouse that roared, and Rismark will be the next Westfield, an example of how Australian real estate technology can match the best that the world can offer and prevail," Brown says.

Rismark is convinced it will deliver and already has a series of funds on the drawing board. Facioni says that Rismark's first fund will avoid any kind of financial engineering, beyond the original innovation of introducing equity finance mortgages, but future funds could be more tailored.

"Given it's a new asset class and it's a new product at the consumer end, we think it's important to keep the fund itself as clean and as pure as possible," he says.

But as consumers get more comfortable with the product, and as investors get more comfortable with backing residential real estate, funds that specialise in particular areas and demographic groups could become a reality.

■ **Names have been changed.*



Home buyers need an easier way into the market.

Photo: PETER BRAIG