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ARE THE REQUIREMENTS OF THE FIRST HOME OWNERSHIP SCHEME USER FRIENDLY?

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Key Points

- The First Home Ownership Scheme (FHOS) is a joint initiative between the Government and Bank South Pacific (BSP).
- The BSP implements the FHOS under a commercial loan arrangement with competitive requirements.
- The FHOS is beyond the reach of the low-income group due to stringent requirements.
- Appropriate policy interventions are required to make FHOS user friendly for all income groups.

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ARE THE REQUIREMENTS OF THE FIRST HOME OWNERSHIP SCHEME USER FRIENDLY?

By Thomas Wangi

The desire to own a house is still a dream for many citizens of Papua New Guinea (PNG) working in the private and public sectors. The Government has introduced the FHOS in partnership with BSP to assist working citizens to buy or build their houses. This paper focuses on one of the findings from the survey of activities of real estate agents in Port Moresby that was conducted by researchers from the PNG National Research Institute in 2018. The survey revealed that potential property buyers engaging with most real estate agents were encountering difficulties in accessing home loans under the FHOS because of the stringent requirements. This paper focuses on the requirements and its challenges.

Under the FHOS, BSP provides home loans for properties with state titles for a 40-year repayment period at an interest rate of four percent. In addition, the borrowers are expected to deposit 10 percent equity for the minimum loan amount of K200,000 and a maximum of K400,000. The scheme is very competitive compared to other home loan products available at BSP. However, when looking closer at the requirements, the FHOS is beyond the reach of households in the low-income group and some in the middle-income group. Most working citizens could not afford the equity component of the loan due to their low wages and salaries. State land is almost exhausted in the cities and towns, affecting property developers' interest in building new houses, resulting in a low supply of houses to the property market. For the first home buyers looking for a new house under six months old, the scheme is not feasible under this circumstance.

In order to make the FHOS accessible and user friendly for most first home buyers, the requirements need to be reviewed. These include paying housing allowances to all pay grades, accepting customary land titles, increasing the housing age threshold, and reducing the equity contribution to below five percent.

The requirements of the First Home Ownership Scheme

The FHOS was introduced by the Government in response to

the chronic housing issues faced by the working population in PNG. In 2014, the Government in conjunction with BSP formally signed an agreement to make FHOS available as a home loan product in the lending market. The FHOS is a joint initiative that provides access to working citizens to flexible and affordable financial arrangements. The objective is to support first home buyers working in the public and private sectors to buy new houses on state lease or construct new houses on vacant state land.

The FHOS is a commercial arrangement between the Government and BSP. The FHOS is not a form of grant, tax break or other concession and therefore the borrowers are required to meet the loan obligations. The Government has allocated K200 million under the FHOS to access housing loans at a lower interest rate. The money is managed by BSP, and is implementing the scheme under the following criteria:

- Minimum loan amount is K200,000 and maximum is K400,000;
- term of the loan is 40 years maximum;
- fixed interest of 4 percent per annum;
- the equity contribution is 10 percent of the purchase price;
- establishment fee of one percent of loan value;
- borrower must be working in the public or private sector;
- property (house or land) must have state title or lease;
- the house must not be more than six months old; and
- the individual must be a citizen of PNG.

The FHOS provides a large incentive home loan for people looking for their first home compared to the BSP's standard home loan, where equity contribution is 20 percent, interest rate is almost 9 percent, repayment period is below 30 years, including various fees and charges. However, borrowers should be mindful of other important terms and conditions of the FHOS. For example, the house is restricted to owner's occupancy only. Furthermore, there are certain restrictions on the resale or refinancing of the loan.

This paper focuses on four requirements: minimum loan of

K200,000 and maximum of K400,000; state title; house less than six months old; and 10 percent equity contribution. Other requirements will be discussed in subsequent papers.

The challenges with the First Home Ownership Scheme

The interest in home ownership and affordable loan products has been relatively high since the introduction of the FHOS in 2014. The majority of loans processed are mostly in Port Moresby, largely due to market size and increased interest by property developers (Loop PNG, 2016). The interest in other cities and towns also remains high, from young professionals to long-serving employees in both the public and private sectors. However, in reality the FHOS is considered to be beyond the reach of most working citizens due to its stringent requirements. The real estate agents have expressed their concerns on strict requirements in a recent survey conducted by the National Research Institute on the activities of real estate agents in the property market in Port Moresby. The obvious beneficiaries are the private property developers because one requirement is that the house must be six months old, which developers are able to meet. However, the real estate agents deal with existing housing stock in the property market, of which most are more than six months old.

- **Minimum loan amount is K200,000 and maximum is K400,000:** The minimum loan amount of K200,000 is beyond the reach of most working citizens in the public sector. According to a study by Wangi and Howes (2014) on PNG's public sector pay scales, most citizens working in academic institutions, government departments and statutory authorities earn relatively low gross incomes, compared to those working in state owned enterprises. The gross incomes attract significant deductions such as tax and superfund. The deductions put pressure on the borrower's ability to make monthly loan repayments over the 40-year period. Given the high cost of living in the cities and towns, the low-income and some middle-income earners will struggle to meet monthly repayments.
- **Property must have a state title:** The state land comprises at least three percent of the total land in PNG and is becoming almost exhausted in the cities and towns. The study by Wangi and Ezebilo (2017b) found that land was a major requirement of building a house. The private property developers prefer to invest in state land because it is secure and has clear land titles. However, the depletion of state land discourages property developers from building new houses in the country. The low supply of new houses in the property

market relative to demand increases house prices in major cities like Port Moresby.

- **The house must not be more than six months old:** It is in the best interest of the first home buyer to have a new house. However, the buyer might find it difficult to access a six month old house because the rate at which new houses are constructed has not been able to match demand. The efforts by developers to build new houses are affected by a shortage of state land, inaccessibility of registered customary land, inadequate trunk infrastructure services, the high cost of building materials, and inadequate government support. Furthermore, the Government's attempt to build new houses for public servants in several housing projects under the FHOS such as the Duran Farm in Port Moresby has not worked well (Nao and Ezebilo, 2017a).
- **The equity is ten percent of the purchase price:** Equity is the borrower's own contribution towards the home loan, and can be sourced from employer assistance, superfund, or/and cash deposits. The employer assistance is rarely available in both the private and public sectors, while accessibility of superfund is regarded as the worker's last savings option. This implies that if the worker exhausts his/her superfund savings through the FHOS, and somehow the loan is at default, then the worker will lose badly in this scenario. The cash deposits sound applicable, but that is determined by the worker's ability to save. Wangi and Howes (2014) found that most workers were paid below the gross income of K40,000 per annum. In order to qualify for the minimum loan amount, the workers must contribute K20,000 equity. This looks unrealistic given compulsory pay deductions and commitments attached to the pay.

Potential policy interventions

The FHOS is an initiative of the Government to address affordable housing issues in PNG, mainly targeting first home buyers. The workers need to make certain sacrifices to own a house in the current market conditions. Even some of the existing requirements need to be reviewed in order to make FHOS user friendly amongst the entire workforce in the country. Some of the interventions that could be adopted include:

- **Pay housing allowances:** The minimum home loan amount is beyond the reach of most low and some middle-income earners, and therefore clearly there is a scope for paying housing allowances to all pay grades. All workers regardless of their pay scales should receive housing allowances. Wangi and Ezebilo

(2017) suggested that the housing allowance should be at least 30 percent of base salary, in line with international housing affordability criteria. This would help working citizens to make timely loan repayments.

- **Accept customary land titles:** The state land is almost exhausted, while the private property developers wish to invest in the state land that has proper titles. As the supply of state land is almost fixed, the only option is to find a way to release customary land to the formal market. However, most investors would not invest in customary land because of insecure tenure. This makes it important for landowners to register their customary land through the Voluntary Customary Land Registration (VCLR) process. The commercial banks such as BSP should consider accepting customary land titles to assist first home buyers to access home loans through FHOS. The VCLR is a legal process and supported by the *Incorporated Land Group Act 1974 and the Land Registration Act 1981*.
- **Increase housing age limit:** There is a need to review the age limit from six months to five years. The size of the property market in PNG is small, implying that the opportunity to buy new houses is restricted. There are only a few private property developers building and supplying new houses, especially in Port Moresby where the housing demand is high. Therefore, it is important to consider the existing housing stock in the property market as well. The increase in age limit to five years provides an opportunity for first home buyers to access houses freely in the property market provided by the developers and real estate agents.
- **Reduce equity contribution:** The equity component is the 10 percent of the sales price of a house, which most workers may find difficult to afford. For example, the lowest sales price for a house in Port Moresby is around K300,000. Most working citizens may not be able to pay the 10 percent (K30,000). Therefore, the Government and BSP should consider reducing the equity contribution to below five percent. This might provide more households with the opportunity to access the FHOS.

Conclusion

The FHOS provides a competitive option for interested first home buyers to access a home loan with BSP. The loan has the potential of helping low and middle-income groups to buy or build their own houses. Many workers find it difficult to access affordable and quality housing under the FHOS because of the stringent requirements. The FHOS that was established by the Government to assist working citizens to buy their own houses is a step in the right direction. However, considering the high house sales prices and the stringent requirements, most workers may find it difficult to benefit from the FHOS. In order to make FHOS affordable and user friendly for first home buyers, the requirements need review. These include; paying housing allowances to all pay grades to meet loan repayments; accepting customary land titles to accommodate increasing demand for land by private property developers to build new houses; increasing housing age limit to freely access houses provided by developers and real estate agents in the property market; and reducing the equity rate to facilitate first home buyers to afford equity contribution.

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