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Deputy Michael McGrath  
Leinster House  
Dublin 2

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Dear Deputy McGrath,

I am writing to you in response to your recent letter concerning the Help to Buy scheme. In advance of the Budget, I was consulted only on the specific issue of whether a tax rebate would qualify in meeting the deposit requirement for first-time buyers under the Central Bank's macroprudential mortgage rules. As you know, these rules are designed to enhance the resilience of both borrowers and the banking sector. I confirmed that a tax rebate would be a valid contribution in meeting the deposit requirement, together with the own funds raised by a first-time buyer of a new home.

You requested the Bank's views on the properties of the scheme. In my pre-Budget letter to the Minister for Finance, I advised that "any fiscal measures in support of the Government's housing strategy should be sufficiently targeted to avoid material aggravation of current distortions in the residential property sector".

A comprehensive assessment of the scheme would require a full-scale evaluation project, including quantitative analysis of its impact on demand and supply conditions in the housing sector. Such a full-scale assessment of individual fiscal measures falls outside the scope of Central Bank's economic advisory function, which is typically confined to macroeconomic and financial stability topics.

That said, let me make a few observations. First, the standard criticisms of any subsidy scheme are that: (a) it runs the risk of displacing activity that would still occur in the absence of the scheme: some fraction of the households receiving the subsidy would have bought the same property in the absence of the scheme; and (b) if there is an insufficient supply response, raising demand in a given segment of the housing market will just tend to put upward pressure on prices, with the sellers of properties effectively gaining more than the recipients of the subsidy.



Second, at the qualitative level, it is possible to identify a positive supply-side mechanism: if developers of starter homes are currently finding it difficult to raise equity and debt funding due to a concern among investors and lenders that there is a lack of sufficient effective demand for such types of new homes, the easing of the financial situation of qualifying first-time buyers may support a greater level of construction of new homes. This mechanism has greater salience in a post-crisis environment, since the reliance of developers on external funding is currently greater than in previous periods due to the losses sustained during the property crash. In assessing the supply dimension, it is also important to bear in mind the inevitable lags in the production of new homes and various other factors that are currently inhibiting the construction of new homes.

Third, in assessing the impact on the financial health of the household sector, there is a positive impact on the first-time buyers receiving the subsidy. However, some recipient households may opt to borrow more in order to purchase more expensive properties, such that total household debt may expand under some scenarios. The reduction in the minimum deposit condition from 80 per cent to 70 per cent is a positive step in mitigating the risk of additional household borrowing in response to the scheme.

Assessing the net impact of these different mechanisms would require full-scale quantitative modelling. It is also important to be aware of the relative size of this segment of the housing market: according to CSO data, first-time owner-occupiers bought 756 new homes (out of total sales of new homes of 2,368) in 2015, while first-time owner-occupiers bought 8,340 existing properties (out of total sales of existing properties of 34,695) in the same year.

Finally, many fiscal measures have a distributive element: it is up to the political system to make the relative assessment of the distributional impact of this scheme, compared to other potential allocations of this funding.

Yours sincerely,