WORKSHOP ON HOUSING FINANCE IN TRANSITION ECONOMIES

Paris, 19-20 June 2000

Summary Record of Meeting

This document prepared by the Secretariat is circulated for information for the meeting to be held on 10 - 11 October 2000.
I Introduction

1. The establishment of a functioning housing finance system is of major importance for economies in transition. Until now, the old housing systems have been mostly disposed of: the government has ceased being a dominant provider of housing, and land and dwellings have been returned to, or placed in, private hands. However, new systems, which should be based on a market mechanism, have yet to become fully operational. In order for market-based housing transactions to be active, the financial mechanism is a major factor, as homes are usually too expensive for the public to purchase with cash. Given that housing is one of the basic needs of the public, and is an essential social policy of any government, establishing a well-functioning housing finance system is an important policy issue for transition countries now.

2. Against this backdrop, a Workshop on Housing Finance in Transition Economies was held on 19-20 June 2000 in Paris. It was organised by the Directorate for Financial, Fiscal ad Enterprise Affairs (DAFFE) as an outreach activity of the Committee on Financial Markets under the framework of the Centre for Co-operation with Non-Members (CCNM) Programme. The workshop brought together more than 80 officials and experts from 10 non-Member transition economies and 15 Member countries as well as the World Bank (see attachment A).

3. The objective of the workshop was two-fold. First, it intended to review the status quo of housing finance systems in transition countries and to assess the steps needed to develop such systems. Second, the workshop aimed at creating a forum for relevant officials and experts to exchange information and to learn from each other's experiences. As a kick-off, the meeting provided an overview of the major issues to be addressed to facilitate the establishment of market-based housing finance systems in transition economies. These include the development of the housing loan business, the necessary institutional arrangements and funding strategies, as well as the practical steps to be taken and the role of the government (see attachment B). The workshop was chaired by Mr Eigil Mølgaard, Deputy Secretary, Danish Ministry of Economic Affairs.

II Housing Finance in Transition Economies: What Is It and What Should It Be?

Main features of well-functioning housing finance systems

4. There are a variety of well functioning housing finance systems in advanced market countries. They constitute an important segment of the financial markets. Housing loans outstanding account for 20 to 60 percent of GDP. Variations in the housing finance systems tend to reflect the particular economic and social contexts in which these systems have evolved. In fact, the housing finance systems in advanced
market countries have a long history. For example, many mortgage banks in Europe, such as Germany’s Hypothekenbank and the Crédit Foncier de France, were founded in the middle of the 19th century. Fannie Mae (formerly the Federal National Mortgage Association) of the United States was established in the 1930s. The housing finance systems that have evolved all work well in their own situations, and have been influenced by the economic and social developments peculiar to their respective countries as well as their particular geographical and demographic characteristics. Further, as the operating environments change owing to advances in information technology and the globalisation of economic and financial markets, these systems continue to evolve.

5. Among the various housing finance systems that exist in advanced markets countries, some common models can be identified. One such model is the “Southern European” model (e.g. Spain, Italy and Greece). Housing finance markets in these countries are characterised by very high levels of owner-occupation, low transaction levels, and less favourable terms for mortgage credit.

6. These markets differ in many respects from those served by the so-called “home-owner” model. The latter tend to be characterised by high transaction levels and more favourable credit facilities, supported by highly liberalised financial markets. This type of housing finance system is typically found in the Scandinavian and English speaking countries, in which the owner-occupation ratio is around 60 to 70 percent. For example, the United States has developed the world-largest housing finance market with very sophisticated financing systems. Historically, the primary (i.e. origination) mortgage market in the United States has been dominated by deposit-taking institutions (thrifts and more recently banks) and mortgage brokers/servicers. After origination, mortgages are either held in portfolio or sold into the secondary market where they are pooled and repackaged as mortgage-backed securities. Three government-sponsored enterprises (GSEs) -- Freddie Mac, Fannie Mae and Ginnie Mae -- are the primary agents in the secondary market. The first two agencies finance mortgage loans by issuing mortgage-backed securities. Ginnie Mae, a department of the US Department of Housing and Urban Development, provides a full faith and credit guarantee on pools of loans guaranteed by the Department of Veterans Affairs or insured by the Federal Housing Administration, but does not itself issue securities. Secondary markets in the United States account for roughly half or outstanding home mortgage credit and in recent years have accounted for some three-fourths of the net increase.

7. The third model is called the “balanced tenure” model, in which a relatively larger segment of the population tends to live in rental residences and therefore the owner-occupation ratio is as low as 40 to 50 percent. Housing finance markets in Germany and Austria are examples of this model. In these countries, housing finance systems are rather specialised, highly regulated and integrated, which creates more stable but less active markets than those in countries featuring the home-owner model.

8. During the session, several factors were identified as essential for a housing finance system to work effectively. First, the most basic infrastructure is a legal system that supports mortgage transactions. It includes the system for recording titles that not only establish property rights appropriately but also ensure the ability to transfer titles at a minimum cost, and also includes efficient foreclosure laws and practices. These are important prerequisites to make it possible for houses to act as effective collateral.

9. The second factor identified as indispensable for any housing finance system is adequate funding. There are two basic kinds of funding sources in practice: deposits and securities markets. At least one of them needs to be available to channel public savings to housing finance. It was pointed out in this regard that private money had to be utilised, as a healthy housing finance system could not be maintained only with public funds.

10. Third, an appropriate regulatory structure should be in place. Housing finance should be viewed as a means to an end, i.e. homeownership. Given the relative importance of housing policy, the
government is typically involved in any housing finance system in one way or another. However, housing finance is also part of the overall system of capital allocation. Therefore, regulations concerning housing finance should be designed and implemented in a way that does not distort the efficient allocation of capital in a society. The experience of the United States shows that housing finance has a potential spillover effect to the whole capital market. Thus, the first asset-backed securities issued in the United States were the mortgage-backed securities developed by GSEs.

11. The fourth factor needed to ensure that any housing finance mechanism functions properly is macroeconomic stability. A relatively stable macroeconomic environment is especially necessary for housing finance given its long-term nature.

Current situations and strategies of transition economies

12. Under the Communist regimes of many Central and Eastern European countries, the government was responsible for providing housing for the public. As a result, transition economies tend to have relatively large housing stocks. The number of dwellings per capita is almost comparable to that of advanced market countries. However, the housing markets are not very active, when compared with those in advanced market countries.

13. Inactivity of the housing markets in transition economies can be attributed to several factors. Among them is a very high owner-occupation ratio. In these countries, except for the Czech Republic, Latvia and Poland, owner-occupied housing accounts for over 90 percent of the housing stock. This large share is obviously the result of privatisation of real estate property in the early 1990s. It should be noted, however, that there are problems with the quality of many of the existing dwellings. These problems, which were all inherited from the former Communist regimes, include too small size, poor construction, poor maintenance and insufficient infrastructure. This situation creates significant potential demand for higher quality housing. However, the supply of such housing is insufficient. As part of the economic transformation process, the governments in these countries have largely pulled out of the housing construction business, but private sector activity has not yet expanded sufficiently to compensate. Consequently, the supply of quality housing is constrained and the price is too high to be affordable for the typical homebuyer. Moreover, a good housing finance mechanism, which would help people to acquire such housing, has not yet been developed in transition economies.

14. There was a housing finance system under the former regime. Typically, state-owned banks were responsible for extending housing loans with very long maturities and very favourable fixed interest rates, with no required collateral or downpayments. However, this system was obviously not sustainable, especially once the government stopped providing financial support after the economic transformation, and it was completely destroyed by high inflation during the early years of the transformation. In lieu of direct support, many governments have made considerable efforts to encourage market transactions by introducing various financing schemes. The development of market-based housing finance systems has become an important policy objective for all transition countries.

15. The efforts in various transition countries were presented at the meeting. In Poland, the Mortgage Fund was established in the early 1990s as a liquidity facility to finance inflation-proof mortgage loans (mostly dual-indexed mortgages) made by banks on a commercial basis. The Act on Mortgage Bonds and Mortgage Banks adopted in 1997 has introduced a German-type mortgage bank system in which specialised mortgage banks may raise funds by issuing mortgage bonds against their mortgage assets. At present, two mortgage banks are in operation and mortgage bonds were first issued in June 2000. In addition, there are two different contract saving systems in Poland. However, one was introduced in 1995 and has granted an insignificant amount of loans to date. The other system was created in 1997 but
has not yet begun operation, as the government intends to reorganise and unify both contract saving systems.

16. In Slovenia, commercial banks are currently the primary suppliers of housing loans to individuals, accounting for almost 60% of the market. However, a large portion of the loans are short-term credits, and are not secured by mortgage as collateral. Only 16% of them are mortgage loans, though the share is increasing year by year. The remaining 40% of housing loans to individuals have been granted by the Housing Fund of the Republic of Slovenia. Established in 1991, the Fund extends credit for purchase or construction of dwellings by individuals and for construction of social-rented dwellings by non-profit housing organisations and local communities. The Fund receives a government subsidy which it uses to provide long-term housing loans on favourable terms. In addition, a contract saving system, that is called the National Scheme of Money Saving for the Purchase of Apartments, was introduced in July 1999. The Scheme is run by selected banks with the support of the government subsidy granted to participating individuals through the Fund.

17. Thanks to these efforts, market-based housing finance systems have emerged in these countries in recent years, though they still remain in their infancy. The current volume of housing loans outstanding, is nominal -- less than 5 percent of GDP -- for all transition economies. The low level of transactions certainly reflects the short history of market-based finance and also inactive property markets that can be attributed especially to significantly high prices. However, various other obstacles to the development of the housing finance markets have also been identified. First, as many delegates pointed out, the income level of the population is not yet high enough and only a small portion of the public is regarded as financially eligible for loans. Second, relatively high economic uncertainty in transition economies has discouraged both borrowers and lenders from arranging long-term credit. Third, the legal infrastructure still needs to be improved. Some relatively advanced countries like Poland have already set up the necessary legal and institutional infrastructure for housing finance, but many others have not. Fourth, an underdeveloped financial sector was also regarded as an important challenge for the development of housing finance. For example, the lack of efficiency in the banking sector allows a huge gap between deposit and lending rates, which effectively deters households from acquiring housing loans. Finally, it was also pointed out that there were problems of mentality: many people in transition countries tend to long for exceptionally high-quality housing regardless of its affordability, but at the same time put a high priority on purchasing other durable goods such as cars.

III Development of the Mortgage Loan Business

Practical aspects of mortgage system designing

18. The mortgage lending business entails certain risks that must be properly managed if the business is to be successful. These risks can be categorised into two types: general macroeconomic and legal/regulatory risks, and operational risks.

19. As repeatedly pointed out at the meeting, the existence of an adequate legal and regulatory environment that supports a mortgage lending system is an essential prerequisite. There must be laws in place that secure private ownership of land and houses and the ability to use the title to property as security for a mortgage. The legal framework needs to be supported, particularly by the registry system that records the history of title and any liens against a property. Advanced market countries such as Denmark and Sweden have a long history of real estate registration in which every square metre of land has been registered and, moreover, been evaluated for tax purposes. Of importance as well is a foreclosure system that enables a lender to foreclose on a mortgage smoothly if the loan is not repaid.

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20. The establishment of an adequate legal system is obviously the responsibility of the government. In most transition economies, relevant laws have been in large part already introduced. However, effective enforcement is not necessarily in place. Participants reported that in some transition countries the registration of the title to the land book took one year or more. The creation of an appropriate legal environment usually takes time. It was suggested that weak legal enforcement might be supplemented to some extent by mortgage insurance that is often supported by the government.

21. Unstable macroeconomic conditions also create a significant risk beyond the control of the housing loan businesses. Among other factors, high inflation risk is often regarded as a major obstacle to any long-term financial industry, including housing finance. There are alternative mortgage instruments available to deal with interest rate fluctuations. For example, Mexico has invented UDI mortgage loans (inflation indexed loans) and FOVI mortgage loans (dual-indexed mortgage loans linked with both the inflation and minimum wage rates) through its experience of the “Tequila Crisis” in 1994. It should be noted, however, that such loans help lenders avoid inflation risk principally by passing the risk on to the borrowers, and thus the loans may be less attractive to borrowers than standard fixed-rate products. This is probably why adjustable-rate mortgage products are not widely used in advanced market countries, except for the United Kingdom and Ireland. It was suggested that the risk for borrowers might be mitigated by the use of a counter investment fund, though this would also increase the financial burden for borrowers to acquire loans. It is also possible that a government can assume the interest rate risk. In Sweden, the government at one point had guaranteed a fixed interest rate of 3.25 percent for housing loans. However, this measure has been abolished due to the heavy budgetary burden and the distorting impact on the financial market when market rates rose. The direct solution to this problem is the adoption of prudent macroeconomic policies to stabilise macroeconomic fluctuations.

22. Another macroeconomic or market risk related particularly to mortgage finance is volatility of the property price. Uncertainty related to the future price of land and housing deteriorates their value as collateral for long-term credit. This leads to inefficiency in the mortgage loan market by lowering loan-to-value ratios and possibly necessitating other types of collateral, as is the case in many transition countries. The remedy against this risk is stabilisation of price volatility, which requires prudent macroeconomic management as well as the establishment of a deep property market.

23. In addition, some participants stressed that the availability of appropriate funding for long-term credit is also an important prerequisite for housing finance systems to work. One of the solutions is the creation of mortgage bond markets. As mentioned below, a number of transition countries have recently introduced or planned to introduce legislation for mortgage banks and mortgage bonds, similar to that of Germany and other continental European countries.

Effective management of the mortgage loan business

24. The risks discussed above are beyond the control of individual businesses and thus are left to central governments to handle. There are, however, other risks that housing loan providers themselves have the primary responsibility for managing in the course of their normal business operations, although even here the government can also provide some support. These risks include, in particular, credit risk and operations risk.

25. The proper management of credit risk is a key ingredient for the successful provision of housing loans. In order to avoid loss of borrower defaults, the logical thing to do is to avoid taking excessive credit risk, which can be done by limiting credit extensions to the highest quality borrowers subject to high equity requirements. However, this strategy has its downside; namely, it lowers the overall return on the portfolio and limits its business potential. Thus, it is necessary instead for lenders to adopt a risk management
strategy that recognises the necessity of taking some measure of credit risk in order to achieve the desired level of profitability and market potential.

26. Credit risk management includes three major elements. First, there is the requirement for a proper assessment of a customer’s ability and willingness to pay for the loan for its duration. A lender needs to develop the necessary criteria, which should take into account the unique characteristics of the local market. To the extent possible, the assessment should be objective, based on data obtained from a reliable independent source, and verifiable in some way. Many advanced market countries such as Canada have a comprehensive network of credit bureaus that retain electronic data on consumers, retail, finance and other accounts to keep track of missed payments, which is obviously an important supporting infrastructure for the housing loan business. In contrast, the availability of borrower data is still limited in transition countries. For example, unreported income is often too important to ignore, but difficult to rely on without any formality. Contract saving programmes are useful in this regard, as they create a credit record of regular payments in themselves.

27. The second element is equity. A fair equity portion helps to motivate borrowers to continue to pay, and also helps the lender to recover damage in the event a borrower defaults. However, in transition countries where the necessary detailed data are often unavailable, it is not easy to establish an efficient equity requirement (or LTV ratio). The third element in credit risk management is the availability and use of other kinds of collateral when necessary. Mortgage insurance or use of a counter-risk pool of funds as suggested in the previous section can be beneficial in mitigating credit risk. In Canada, a public mortgage loan insurance programme was established in the early 1950s and has since helped one in three Canadians acquire a home. Borrower education is an important source of guaranty. Maintaining contact with borrowers through the provision of occasional financial advice not only can help borrowers understand the value of payments but it is an effective way to reduce the default risk.

28. Operations risk also needs to be effectively managed. It occurs at all levels of activity in a mortgage finance operation. If the risk is high, for example, because of operational errors and fraud, the operational cost soars and the business cannot be run at a profit. There are a few important ways to mitigate operations risk. The first is training. A well-trained staff makes fewer errors and can handle higher volumes of transactions. A second step is use of technology, which increases the volume of operations that can be managed with the same staff, reduces errors and fraud and also facilitates the collection and analysis of data. It should be noted, however, that both training and technology are likely to increase costs in the short term, though over time they should become effective in reducing operations cost.

29. Simplicity is another useful tool to reduce operations risk. Complex products are more difficult to manage and thus are more likely to increase operational cost. Standardisation of documents and operations should lead to lower operational cost, at least in the long term. In addition, qualified external and internal auditors, as well as the enforcement of quality control by checking samples of loans regularly, are also important in avoiding operational problems.

IV Institutional Arrangements and Funding Strategies

Alternative funding strategies and risks

30. In order to develop a well-functioning housing loan business, it is essential to establish a system to raise financial resources sufficient both in quantity and quality to fund loans. Various instruments to do so have been developed in advanced market countries. These instruments can be placed into two categories: deposits from the public and products of capital market facilities.
31. Retail deposits are still the primary financial resources for housing loans even in advanced markets countries. For example, in EU countries, deposits account for 62 percent of the funding of mortgage loans. Deposit financing is even more dominant in transition countries, given that issuance of mortgage bonds has started only recently.

32. A special scheme to mobilise retail deposits for housing loans is the contract saving system. Germany’s bauparkassen is the typical example, which many transition countries have introduced to develop housing finance. Under this system, a saver enters into a contract with a savings institution to undertake savings up to a specific sum according to a set schedule. Upon the conclusion of the savings period, the saver acquires the right to get a loan for a prescribed purpose at a predetermined, fixed interest rate. Proponents of contract savings schemes suggested that this system has various advantages. Savers/borrowers can be largely immune to interest rate fluctuations. Credit records of savers/borrowers can be established by the system itself during the saving periods. From a macro point of view, a contract savings system encourages people to undertake long-term saving and increase the aggregate savings level in a country. The system can be regarded as a transparent basis for subsidies, as the subsidy is directly allocated to individuals for housing. These merits are particularly important for transition economies, which still face macroeconomic uncertainty and difficulty in getting credit records for individuals.

33. However, during the meeting, other participants noted the disadvantages of contract savings schemes. For example, due to their long-term nature, contract savings schemes may not be flexible enough when confronted with changes in the economic environment. Moreover, in order to attract a fair number of savers, contract savings schemes normally need government support in the form of interest rate subsidies, which are likely to create substantial budgetary burdens. The schemes may also cause a difficult political problem, inasmuch as they will not yield immediate result on housing due to the required build-up during the initial saving period. While such transition countries as Slovakia and Slovenia are promoting this system to expand housing finance, Poland is trying to step out of it.

34. Capital markets are an alternative source of funds for housing loans that have recently increased in importance in many advanced market countries. There are generally two ways to raise funds from capital markets for mortgage loans: mortgage bonds and mortgage-backed securities. Mortgage bonds issued by mortgage banks have a long history in Europe, dating back more than 100 years. Currently, Germany has the biggest market, amounting to EUR 930 billion. The EU UCITS Directive (Article 22 IV) provides a definition of mortgage bonds. It was argued, however, that the Directive provides only minimum standards: more detailed regulations, such as those on investment, asset and liability valuation, loan-to-value ratio, cover register and trustee, would be necessary to protect the reputation of the bonds and develop the markets. As a result, actual regulations differ across countries.

35. Mortgage bonds are gaining more attention as an important funding source for mortgage loans, not only in Western Europe but also in Central and Eastern European countries. Mortgage bond legislation has been introduced in the Czech and Slovak Republics, and in Hungary, Poland and Latvia, and has been drafted in Estonia, Bulgaria and Russia. In the former five countries, actual issuance of the bonds has also begun, although the outstanding volumes remain trivial, with the exception of the Czech Republic, which has carried out 17 issues, amounting to EUR 520 million. To a large extent, it is a condition for a bond market that long-term saving is institutionalised by, for example, pension funds and life assurance. This is, however, not the case in most transition economies.

36. There was discussion during the meeting, however, concerning the priority that should be given to mortgage bond legislation as a means of developing housing finance in transition countries. It is clear that bond financing has the merit of addressing the maturity mismatch associated with long-term housing loans. It was also pointed out that mortgage bonds could be the tools to connect expectation of lower inflation with current interest rates when the financial market has an inverted yield curve, as is currently
the case in Hungary. Nevertheless, some participants argued that given the relative importance of deposit finance (even in advanced market countries) and the underdeveloped legal infrastructures and capital markets in transition countries, the priority for policy should be the development of housing loan originations, whatever the means of finance. There was also broad consensus that there is no single, successful model that can fit all transition economies.

37. In contrast to mortgage bonds, mortgage-backed securities have not been popular among European countries, compared with the United States. Some reasons for this were suggested, including a less favourable weighting in capital requirements, lack of government-backed agencies like in the United States, lack of standardisation, the existence of competitive on-balance sheet funding instruments, and so on. No issues of mortgage-backed securities have been reported by transition countries.

**Institutional arrangements**

38. Various kinds of financial institutions can play a role in the housing finance market. These institutions can be largely divided into two types: specialised institutions and non-specialised ones. In many countries, one or more financial institutions that specialise in housing finance have been established, though their functions vary considerably.

39. Mortgage banks, such as those developed in Scandinavia, Germany and other continental European countries, are among the most common types of specialised institutions. Though they have historically financed their loans with retail deposits, nowadays they are closely linked with mortgage bond financing. Mortgage banks are often given the exclusive right to issue mortgage bonds, but, in turn, are subject to tight regulation, especially in terms of their investment. For example, France established legislation in 1999 to introduce a new type of mortgage lending institutions (sociétés de crédit foncier) that are allowed to issue mortgage bonds (obligations foncières). In return for the privilege to issue the bonds, these institutions are subject to strict regulation and special insolvency procedures to keep ratings on the bonds high. They are also subject to special supervision by a specific supervisor who is required to report to bondholders for each institution, in addition to the banking supervisory authority (Commission Bancaire). As mentioned above, several transition countries have enacted or drafted new legislation to introduce mortgage banks coupled with a mortgage bond system.

40. Another example of specialised institutions is the bausparkassen, developed especially in Austria and Germany. Bausparkassen are the institutions specialised in running these countries’ contract savings systems. While contract savings can be offered by non-specialised lenders such as commercial banks, bausparkassen operate the closed scheme in which they provide housing finance with funding obtained from savers under the saving contracts. The closed scheme is said to be beneficial in isolating the entire system from interest rate fluctuations, though it may suffer from liquidity problems in the absence of a steady expansion of the business. In particular, when market interest rates rise, the scheme is likely to face difficulty in securing enough deposits to finance loan demands. Some participants argued, therefore, that bausparkassen might not be so suitable for transition countries until the latter succeed in stabilising their inflation rates. Others pointed out that the system worked adequately in Germany even when the economy was unstable before and after World War II.

41. In spite of widespread practices to establish specialised institutions, non-specialised ones, such as commercial banks, co-operatives, life assurance companies and pension funds can also be important players in the housing loan market. In fact, in EU countries, non-specialised institutions account for more than 60 percent of mortgage markets, and, in particular, commercial banks hold about 40 percent. The strengths of non-specialised institutions include flexible risk management using various types of financial products as well as cross selling. It was reported that in some European countries, mortgage loans were
made at a loss, which was compensated by profits from other activities such as credit card businesses supported by long-term relationships with the mortgage borrowers.

42. In transition countries, savings banks, which were specialised for individual customer businesses rather than for housing finance, used to dominate the market. While they remain important players in some countries in general, their business has diminished due to unstable macroeconomic development, large shares of non-performing assets and the abolishment of government support. The establishment of specialised institutions in transition countries is often intended to compensate for the disfunctioning of non-specialised financial institutions in the housing finance business. Estonia seems to be the exception in this regard. There, the major commercial banks have significant foreign capital and thus tend to have sufficient cash available for housing loans, so there is no real need for specialised institutions or bond financing.

43. In addition, it was also pointed out that the distinction between specialised and non-specialised institution has become less important. In some countries, universal banks and specialised institutions such as mortgage banks and *bausparkassen* tend to be integrated in groups or conglomerates, so that various financial services can be offered at one window.

V Practical Steps for Establishing Housing Finance Systems

44. Housing is one of the basic needs of the public, but it is very expensive. This is a major reason why governments should play a role in the housing and housing finance sectors. Housing costs anywhere from 2.5 to 6 times average annual income in advanced market countries. It is yet more expensive and indeed hardly affordable for lower-income people, who are often in the majority in transition countries.

45. The high cost of housing is accommodated by savings, subsidies and finance. In transition economies, however, finance is currently scarce, which results in the heavier use of savings and government subsidies than in advanced market countries. In order to approach the situation of advanced market countries, the direction of reform that transition economies should take is to increase the use of finance and reduce that of savings and subsidies.

46. Heavy dependence on savings to accommodate housing is attributable largely to two factors: an extremely high home ownership ratio and low energy efficiency. Typically, households in transition economies spend 20 to 30 percent of their income on energy consumption. This high ratio is partly a result of relatively high energy prices (many transition countries import energy) and also old-fashioned, low-quality facilities (bad isolation and circulation systems). Under these circumstances, housing subsidies are likely to be used up in paying for utilities. Most of the population in transition countries own their residences, thanks to privatisation in the course of economic transformation. However, these residences are in a state of rapid devaluation, because households do not invest in maintenance. This is not only because the cash available for housing expenditures is mostly directed to energy expenses, but also because the low marketability of houses does not encourage households to invest in their residences. Therefore, reform is of urgent necessity to increase energy efficiency and to remove obstacles (for example, land use control) for residences to be placed on the market. The latter is also important for the development of the financial market, as the owners could issue debt against the marketable assets.

47. Government subsidies for housing are common even among advanced market countries. However, they are particularly significant in transition economies -- often larger than those for health and for education. Clearly the subsidy needs to be reduced. Funds would be better targeted to the limited number of people who really need public assistance, and some transition countries have started to move in
this direction. Also, subsidies should be structured in a way that they complement rather than replace market-based finance systems.

48. In order to reduce subsidies, governments need to make efforts to develop a functioning housing finance system. To this end, establishing an adequate legal and regulatory environment as well as achieving macroeconomic stability should be the priorities for policy. Another important role of government is to assist in the preparation of an effective financial mechanism to mobilise capital for mortgages. This can be done by establishing a system to collect domestic savings. For example, in Japan, when there was a serious shortage of housing after World War II, the Government Housing Loan Corporation (GHLC) was established to provide for effective housing financing, at a time when the government budget was limited. The GHLC was designed to raise financial resources from the public in the form of postal savings, given that the undeveloped private financial sector was not able to provide long-term, low fixed-rate loans for residential mortgages.

49. In today’s world, however, it may also be possible for lenders to tap the bond market, exploiting technology and globalisation. The establishment of the bond market is beneficial for transition countries not only to attract global capital to their housing finance markets, but also to suppress the high margins that banks are getting in these countries by introducing competition. This would enhance the availability of mortgage finance for a larger portion of the population.

50. Finally, in designing and implementing government strategies on housing finance in the overall context of housing policy, co-ordination among relevant authorities is important. In Estonia, a task force was formed to discuss a consistent policy for the development of housing finance, which involves the Ministry of Finance, Ministry of Economic Affairs, Ministry of Social Affairs, local authorities and practitioners.

VI Conclusions

51. The housing finance markets in transition economies are still in their infancy. In order to establish a full-fledged market-based economy, there is an urgent need for these countries to develop well-functioning housing finance systems. Many transition countries have already made progress toward this end, but none of them has yet reached a desired level. Therefore, they are currently in a position to get the maximum benefit from an exchange of experiences and policy advice from advanced market countries and from other transition countries as well.

52. A number of participants expressed their appreciation for this meeting and considered it to be a timely and useful event. Many of them also explicitly requested the OECD to continue this project. These views were confirmed by the evaluation questionnaire, in which participants gave a ranking of 4.4 on a scale of 1 to 5 (with 5 representing “excellent”) to the question regarding the usefulness of the workshop. All of them asked the OECD to develop this project further.
PROGRAMME

Day 1

08:30-09:00  Registration

09:00-09:15  Opening Remarks

➢  Mr. William Witherell, Director, Directorate for Financial, Fiscal and Enterprise Affairs, OECD
➢  Mr. Eigil Mølgaard, Deputy Secretary, Ministry of Economic Affairs, Denmark

Session I: Housing Finance in Transition Economies: What Is It and What Should It Be?

09:15-10:45  Part A: Main Features of Well-Functioning Housing Finance Systems

• Characteristics of well-functioning housing finance systems
• Minimum requirements for functioning housing finance systems
• Government strategy aspects (subsidies, privatisation, macroeconomic conditions)

Lead speakers:

➢  Mr. Robert Van Order, Chief Economist, Housing Economics and Financial Research, Freddie Mac, USA
➢  Mr. Mark Stephens, Lecturer, Department of Urban Studies, University of Glasgow, UK
➢  Ms. Daniela Grabmullerová, Director, Housing Policy Department, Ministry for Regional Development, Czech Republic

10:45-11:15  Coffee break

11:15-12:45  Part B: Current Situations and Strategies

• Overview
• Country presentation (an OECD transition economy)
• Country presentation (a non-OECD transition economy)
12:45-14:30 Lunch break

Session II: Development of Mortgage Loan Business

14:30-16:00 Part A: Practical Aspects of Mortgage System Designing
- Various types of mortgage under alternative macroeconomic scenarios
- Legal and regulatory framework
- Infrastructure support

Lead speakers:
- **Mr. Jose Landa**, Mortgage Director, Auritec-GMAC/RFC
- **Mr. Tim Lassen**, Association of German Mortgage Banks, Germany
- **Mr. Erik Österlöf**, Vice President, Stadshypotek AB, Sweden

16:00-16:30 Coffee break

16:30-18:00 Part B: Effective Management of Mortgage Loan Business
- Practical administration of mortgage transactions
- Business opportunity and associated risks
- Risk management

Lead speakers:
- **Mr. Claude Poirier-Dufoy**, President, Canada Mortgage and Housing Corporation
- **Mr. Inesis Feiferis**, President, Mortgage and Land Bank of Latvia
- **Ms. Debra Erb**, President, Societas, USA
Day 2

Session III: Institutional Arrangements and Funding Strategies: Pros and Cons

09:00-10:30  Part A: Alternative Funding Strategies and Risks

- Funding with debt (deposits, loans)
- Funding through securities (mortgage bonds, MBS)
- Contract savings

Lead speakers:

- Ms. Judith Hardt, Secretary General, European Mortgage Foundation
- Mr. József Csomos, Deputy Chief Executive, FHB Land Credit and Mortgage Bank, Hungary
- Mr. Aloyzas Vitkauskas, Managing Director, Housing and Urban Development Foundation, Lithuania

10:30-11:00  Coffee break

11:00-12:30  Part B: Institutional Arrangements

- Mortgage banks
- Building societies
- Other specialised mortgage lenders
- Commercial banks

Lead speakers:

- Mr. Thierry Dufour, Crédit Foncier, France
- Mr. Andreas Zehnder, Managing Director, European Federation of Building Societies
- Mr. Herbert Pfeiffer, Director, First Construction Saving Bank, Slovak Republic

12:30-14:00  Lunch break

Session IV: Practical Steps for Establishing Housing Finance Systems

14:00-15:30  Strategies, Implementation and Role of Government

- Practical project organisation
- Role of government
- Housing finance systems in overall financial market
Lead speakers:

- Mr. Robert Buckley, World Bank
- Mr. Shunichi Kuwata, Manager, Public Relation Division, Government Housing Loan Corporation of Japan
- Mr. Igor Jakobson, Chairman, Estonian Housing Foundation, Estonia

15:30-16:00 Coffee break

Concluding Session: Future Work

16:00-17:30 Conclusions

- Tour de table: lessons from the workshop
- Future work
- Concluding remarks

Annotations

1. The meeting will take place at the International Union of Railways (Union Internationale des Chemins de Fer; 16 rue Jean Rey 75015 Paris) on Monday 19 and Tuesday 20 June 2000.

2. Speakers should restrict their speech to 15-20 minutes. The strict time constraints are necessary to secure sufficient time for floor discussion on each topic. All speakers are encouraged to provide their more comprehensive presentations in written form.

3. Participants are urged to refer to the note on the issues for discussion for guidance in each session. Speakers are asked to address in their presentations all or part of the questions listed in the above-mentioned note.

4. Delegations from transition economies are requested to nominate one representative who is to present his/her views on the lessons from the workshop at the tour de table during the concluding session.

5. For further information, please contact Mr Takahiro YASUI, Principal Administrator, DAFFE, OECD (tel:[331] 45 24 18 26; fax:[331] 45 24 18 33; e-mail: takahiro.yasui@oecd.org). For organisational or administrative assistance, please contact Ms Lynn Whitney, Administrative Assistant (tel:[331] 45 24 88 36; fax:[331] 44 30 63 18; e-mail: lynn.whitney@oecd.org).
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